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# UTILIZATION OF CORPORATE PROFITS IN PROSPERITY AND DEPRESSION

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# AUTHOR'S NOTE

In the literature on corporate profits, income administration, and cycle theory, there is an unusual conflict in deductive conclusions concerning the merits of surplus accumulation. While statistical studies agree that American corporations have consistently reinvested much of their profits, they by no means agree that stockholders eventually receive these withheld earnings during depression periods. The same data are used to show that the reinvesting of earnings is to the best interest of stockholders, and that the withholding of earnings is to the stockholders' detriment.

The inability to reach satisfactory conclusions is due to a surprising lack of data which reflect the experience of specific companies over a period of years. This study is an attempt to meet the need for a thorough analysis of the earnings of specific enterprises over at least one complete cycle, with the objective of showing how much of the profitable period earnings were reinvested as compared with the amounts paid in cash dividends, how the withheld earnings were invested, and what eventually happened to the investment.

It is an almost impossible task to assimilate and present corporate financial history in a manner which emphasizes income administration except by including formidable and deadening detail without which such a study loses its chief virtue. Inadequate reports, inconsistencies in accounting procedures, lack of comparable data, especially in valuation of properties, and juggling of reserve accounts, surplus balances, and stated capital, are a few of the technical annoyances.

The data presented in this study were assembled while the author was an instructor in accounting at the University of Michigan. Throughout the preparation of the manuscript Professors W. A. Paton, R. G. Rodkey, and M. H. Waterman gave valuable assistance and to them my indebtedness is gratefully acknowledged. Professor R. U. Ratcliff, Assistant Director of the Bureau of Business Research, made available clerical

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# CONTENTS

## APPENDIXES

# LIST OF TABLES

## Chapter 1

# THE PROBLEM OF INCOME ADMINISTRATION

### *Need for Detailed Study of Corporate Income Administration*

From many sources there is voiced a growing desire for more detailed and specific data describing results of operating our corporate institutions. Governmental agencies, tax authorities, students of economics, and those interested in the social sciences generally are inquiring into such subjects as excess profits, size of companies and consequences thereof, dividend policies, marketing procedures and pricing policies, capital structure, payments to labor, methods of issuing securities, amount and nature of corporate surplus, and other detailed factors of corporate life. Particular attention is being given to the problem of the division of corporate income between payments to stockholders and additions to surplus, and to the manner of investing earnings retained. Many believe that maladministration of prosperity earnings by the large corporations contributed greatly to the economic collapse of 1929 and the subsequent depression, and maintain that cyclical behavior may be explained by this process of automatic saving and unwise investing. On the other hand, many writers and corporate officials point with satisfaction to the service performed by surplus reserves in carrying corporations through the years of severe losses.

There are few inductive studies which show specifically how much individual companies have earned over a long period of time, what portion of the earnings were reinvested, or how the retained earnings were utilized. Of even more significance, there are no comprehensive analytical efforts designed to demonstrate whether operating expenses and dividend payments are made possible during a depression by the accumulation of reserves during a prosperous era. In a concluding chapter of a recent publication by the National Bureau of Economic Research, Solomon Fabricant points out the need for further analysis of accounting records and specifically states that we need more

detailed information regarding corporate savings and how the savings have been invested.[1]

Most studies dealing with corporate savings are based upon data compiled by the Internal Revenue Department. S. H. Nerlove, W. L. Crum, and others who have used the data most extensively in studying corporate profits express dissatisfaction with the aggregate figures and indicate a desire for more detailed data.[2] The undistributed profits tax and repeal of the tax are more recent factors tending to focus attention upon earnings and savings of specific enterprises. In his writings upon the undistributed profits tax, A. G. Buehler expressed a desire to obtain data indicating the specific uses of corporate savings in order to deal with the question concerning the extent to which corporate savings have been abused in recent years.[3]

"Accumulated corporate surpluses are widely credited with having cushioned the shock of the depression and statistics compiled by the Internal Revenue Department are used to prove the case. But no one has shown precisely how the surplus has functioned, and some economists are candidly skeptical of the proof submitted, as indicated by the following:

> Prevalent opinion is that business enterprise created employment during the depression by spending accumulated surpluses. Income estimates, which show that income paid out exceeded income produced, have been used to prove this view, but this is a misuse of these income data, which in reality indicate disinvestment, and hence less employment.[4]

### *Detachment of Ownership in Large Corporations*

The problem of corporate income administration is of vital public interest, in contrast to the affairs of single ownerships and partnerships. In theory as well as in practice, whatever a

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[1] W. A. Paton, *Corporate Profits as Shown by Audit Reports*, National Bureau of Economic Research (New York: 1935), pp. 110–11.

[2] S. H. Nerlove, *A Decade of Corporate Incomes* (Chicago: University of Chicago Press, 1932), p. vii.

[3] A. G. Buehler, *The Undistributed Profits Tax* (New York: McGraw-Hill Book Company, Inc., 1937), p. 79.

[4] D. D. Humphrey, "The Relation of Surpluses to Income and Employment During Depression," *The American Economic Review*, Vol. XXVIII, No. 2, June, 1938, p. 223.

personally owned business organization makes belongs to the owner and his motives are rarely questioned, whether he builds a new plant, takes a trip to Europe, or invests his earnings in downtown real estate, government bonds, or South American securities.

The results of operating a corporate enterprise are viewed much more critically because of the vital element of managerial stewardship. In the United States today there are more than half a million corporations which file tax returns with the Bureau of Internal Revenue. Many of these corporations are relatively small semiprivate enterprises, but the "big" companies own a large portion of the aggregate invested assets and they account for more than one-half of all corporate income. Table 1

TABLE 1—PROPORTION OF ANNUAL NET INCOME OF ALL INDUSTRIAL CORPORATIONS PRODUCED BY ONE THOUSAND LARGEST CORPORATIONS, 1920–35

(Amounts in millions of dollars)

| Year | Total Net Income of All Industrial Corporations | Net Income of One Thousand Largest Corporations | |
|---|---|---|---|
| | | Amount | Per Cent of Industrial Total |
| 1920 | $6,899 | $3,612 | 52.4 |
| 1921 | 3,597 | 2,062 | 57.2 |
| 1922 | 6,076 | 3,109 | 51.2 |
| 1923 | 7,453 | 3,831 | 51.4 |
| 1924 | 6,591 | 3,625 | 55.0 |
| 1925 | 8,060 | 4,515 | 56.0 |
| 1926 | 8,337 | 4,899 | 58.7 |
| 1927 | 7,459 | 4,225 | 56.6 |
| 1928 | 8,646 | 5,111 | 59.1 |
| 1929 | 9,456 | 5,889 | 62.3 |
| 1930 | 6,429 | 3,716 | 57.8 |
| 1931 | 3,683 | 2,325 | 63.1 |
| 1932 | 2,153 | 1,565 | 72.7 |
| 1933 | 2,986 | 1,804 | 60.4 |
| 1934 | 4,275 | 2,506 | 58.6 |
| 1935 | 5,165 | 2,579 | 50.0 |

Source: Compiled from *Statistics of Income for 1933*, and *Statistics of Income for 1935*: U.S. Treasury Department, Bureau of Internal Revenue, Government Printing Office, Washington, D.C., pp. 47 and 48, 1933, and p. 22 of 1935. (Number of companies approximately one thousand of the largest. Varies due to classifications. Figures before 1930 adjusted to a basis comparable with later figures.)

emphasizes the relative importance of the large corporations in producing the annual net income of all industrial corporations.[5]

Between 1920 and 1936, 300,000 to 500,000 corporations filed income tax returns each year, yet only 1,000 of the largest accounted for some 55 per cent of the total net income.[6] Two hundred of the very largest corporations were responsible for 35 per cent of the net income, while the next 800 in size produced 20 per cent of the total. The National Industrial Conference Board estimates that the national wealth at the end of 1928 amounted to $360,062,000,000, and year end total assets of the 200 largest corporations aggregated $81,077,000,000 which is about 22 per cent of the estimated total.[7]

The significance and importance of these large corporations and their contribution to our productive capacity are made more vivid when gross revenue figures of corporations are compared with those of single ownerships and partnerships. There are 1,500,000 individually owned and partnership enterprises in this country, according to the last census figures available. The gross sales or production of corporations comprising the whole national income for 1933 was $142,000,000,000, and the gross sales or production of the individual enterprises and partnerships was $30,000,000,000, giving a grand total of $172,000,000,000.[8] From these figures it appears that 1,000 of the largest corporations do nearly 3 times as much business as all the single ownerships and partnerships combined.

Securities of most large companies are traded on organized exchanges and are in general widely held with the total corporate ownership to a considerable degree diffused. The Federal Trade Commission compiled data from 4,367 representative corporations showing the distribution of stock ownership in 1922. From the sample selected, total par value of common

[5] In terminology used by the Revenue Department, these companies are classed as nonfinancial enterprises. Financial enterprises, in the language of the Internal Revenue Department, include banks, insurance companies, investment trusts, building and loan associations, and similar institutions.

[6] Not all corporations reported net income, of course, because a corporation must file a tax return whether it makes a profit or not.

[7] *The Conference Board Bulletin*, No. 38, National Industrial Conference Board, February 25, 1930, p. 303.

[8] *Hearings Before the Committee on Finance, United States Senate on H. R. 12395*, 1936, pp. 887–928.

stock held by officers of the corporations was 10.7 per cent of outstanding common, and management owned 5.8 per cent of preferred stock outstanding.[9]

Separation of active control from ownership is more pronounced in the very largest corporations. R. A. Gordon's recent study based upon the two hundred "giant" industrial corporations which Berle and Means[10] found to be the largest in the United States in 1929, shows that officers and directors of the largest industrial institutions own 3.6 per cent of the outstanding voting stock. However, in 17 per cent of the companies, management owned between 10 per cent and 25 per cent of the voting stock. The author concludes that management alone, on the average, tends to own an extremely small portion of the voting stock.[11]

A recent study of security markets made by the Twentieth Century Fund estimates that in 1930 there were 10,000,000 individual stockholders, and that in 1932 the number had increased to approximately 11,000,000 individuals.[12]

Without critical examination of analytical methods, sources of information, or adequacy of samples, one can accept the general implications suggested by the figures just presented. Large corporations are a dominant element in the United States industrial life. Control and management of much of business activity is delegated to a small group who manage but do not own. *The element of stewardship is ponderous.*

## *Conflict of Interests*

How have the small investors, who really constitute the large majority of common stockholders and who actually own these great corporations, been treated year after year? How succussful have well known corporations been as business entities,

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[9] Federal Trade Commission, *National Wealth and Income* (New York), Table 90, p. 159.

[10] A. A. Berle, Jr., and G. C. Means, *The Modern Corporation and Private Property*, Book 1, Chap. III.

[11] R. A. Gordon, "Ownership by Management and Control Groups in the Large Corporation," *Quarterly Journal of Economics*, Vol. LII, No. 3, 1938, pp. 367–400.

[12] Twentieth Century Fund, *The Security Market* (New York: 1935), pp. 50–53.

and have policies of income administration followed by the management been compatible with desires and best interests of the small owner?

It is easily understood that the ambitions of the management and desires of the many small investors may not always be harmonious. The "profit motive" guides owners under a capitalistic system of free private enterprise, prices, and competition, according to classical economists. In our economic society some 55 per cent of corporate income is produced by large institutions which are about 10 per cent owned by the managers. If profit is the motive, we may ask—profit to whom? Profit to the management appears in the form of high salaries, bonuses, dividends, appreciation of shares owned; and it may also result from inside knowledge of what may happen to the market price of shares, or from personal dealings between the management as individuals and the management as corporation officials. Profit to the small stockholder appears in the form of cash dividends and in market appreciation if he elects to engage in speculative trading.

*Reasons for Surplus Accumulation*

In American financial policy there has long existed the belief that a substantial portion of the earnings should remain in the business, and many reasons and arguments are introduced to justify the practice. Traditionally it has always been regarded as sound policy and a commendable virtue to save for a rainy day, although in recent years the practice has been questioned and even branded as an evil. Most business is subject to cyclical and seasonal influences, and the very fact that earnings are substantial in one period is popularly regarded as evidence that a less profitable or unprofitable season must be ahead. This urge to save, based upon the theory of "what goes up must come down," is discussed at length by Foster and Catchings in *Profits*.[13] Keynes goes even farther with the rainy day idea as an urge to save and in somewhat spicy language suggests that saving becomes an obsession and an end in itself.[14]

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[13] W. Catchings and W. F. Foster, *Profits* (Boston: Houghton Mifflin Company, 1925), pp. 241–43.

[14] H. M. Keynes, *Essays in Persuasion* (New York: Harcourt, Brace & Company, 1932), p. 370.

The most common and plausible reason for minimizing dividends arises in the plea for sheer conservatism. Conservatism in the distribution of corporate income is necessary on three counts. In the first place, the measurement of income is based upon postulates, estimates, assumptions, and judgments made by the accountant, and the reported figures are subject to considerable correction depending upon future events and economic trends which may be beyond managerial control. The difficulty of measuring periodic income is well understood and it is sufficient to say that business executives feel justified in accepting income figures with several grains of salt.

A second and closely related reason why annual income figures need to be regarded conservatively rests upon the arbitrary time intervals commonly used. In capital goods industries, especially, the productive process moves slowly, and it is almost sheer speculation to compute net income for one calendar year. Manufacturers made much of this point in testimony before the Senate Finance Committee before the passage of the Undistributed Profits Tax.[15]

Even if annual reported income figures could be accepted as absolutely accurate, there would still be some justification for conservatism in disbursing dividends because earnings fluctuate from year to year. Business managers point out in this connection that all profits paid out in good years with no reserve to absorb losses in poor years would eventually lead to complete liquidation of the enterprise. This position probably overstates the case, but it is easy to see that lack of working capital might become a serious problem from time to time under such circumstances.

Earnings are reinvested in American corporations because managers and investors alike desire to see their enterprise grow. Corporate management has reasoned that in a growing industry in a young country there must be ample room for expansion; that the business enterprise should invest earnings where the rate of return would be most attractive; and that the proper place is none other than the business itself. This attitude justifies retention of earnings for nearly any purpose and it is therefore considered proper financial policy to withhold current

[15] Testimony of Frederick V. Grier, President of Cincinnati Milling Machine Company, Hearings Before Finance Committee, *op. cit.*, p. 510.

income from stockholders in order to facilitate any of the following corporate needs:

1. Strengthen the financial (working capital) position
2. Increase productive capacity
3. Eliminate an original overcapitalization (squeeze out the water)
4. Make it possible to pay dividends more regularly
5. Strengthen the long run credit position
6. Accumulate reserves as a protection against such hazards as a general depression, a changing demand for products, the possibility of new tax liabilities, and other contingencies
7. Set aside reserves in order to comply with legal requirements for dividends
8. Provide funds for the retirement of corporate securities

Undoubtedly there are other strong motives for reinvesting earnings which are hardly considered ethical even if consonant with sound finance and within the law. The plowing back of profits in order to reduce surtaxes on the income of wealthy stockholders has been much criticized in governmental circles and by those who feel that such procedure is unjust to smaller stockholders who would prefer a cash dividend. Moreover, on occasion surpluses have been accumulated by boards of directors who wished to manipulate the corporation's security prices or in order to speculate in inventories or in securities of other companies.

It is probably true that some managements gave little consideration to the needs or wishes of small investors in formulating dividend policies during the 1922–36 period, and that retained earnings resulted more from selfish reasons than from general conservatism. Dewing suggests that management chooses to expand and therefore to retain earnings in order to satisfy personal ambition, to appease the creative impulse, and to satiate the desire to speculate.[16]

One should not be too severe in criticizing particular industries and specific corporations for retaining substantial portions of their 1922–30 profits even if they were lost in the early thirties

[16] A. S. Dewing, *Financial Policy of Corporations* (New York: The Ronald Press, 1934), pp. 694–97.

because of inventory price declines and idle plant facilities. The motives may have been commendable even if based upon economic fallacies and misconceptions and a popular custom of the times. Moreover, legal considerations, often none too soundly grounded, have had a bearing. The legal fiction which requires a surplus before dividends can be paid in excess of current earnings encourages corporate savings. Particular corporations such as banks and insurance companies are subject to a variety of restrictions upon their dividend payments on the assumption that surplus is necessary for the protection of depositors and policyholders, and they are required by law to accumulate a surplus. Bond contracts of industrial enterprises often provide for restrictions upon dividend payments in order to increase the stock equity as added protection for the creditors.

Many of the reasons given for retaining earnings have little merit, and there is considerable justification for the criticism of corporate savings. However, the chief explanation of small dividends is often overlooked. Much of the corporate saving during prosperous periods is semiautomatic and largely inevitable, and corporate managers may exercise little deliberate choice or control over the portion of earnings retained. When revenue volume is increasing, additional physical inventory is needed and increased unit costs require a substantial increase in inventory investments. Increased sales volume means a greater necessity for increased plant capacity and improved productive processes. When plant capacity is increased there is more pressure to sell, which leads to greater commitments in receivables. In order to profit from rising business volume this process is probably inevitable, and it might prove very difficult for management to avoid the increase in receivables, inventories, and plant facilities. The payment of dividends is considered at periodic dates usually months apart, and the cash balance and current position are likely to appear much more relevant than current income or surplus reserves in determining appropriate action.

### *Effectiveness of Corporate Reserves*

Those familiar with the literature in the fields of corporate finance and accounting will recall any amount of eulogy

on the effectiveness of corporate surplus and the wisdom of retaining profits of prosperous periods in order to pay wages and dividends through depression years. Investors have been taught to pay lip service to the theory that reinvested profits and accumulating surplus reserves will result in a stable dividend rate which redounds to the benefit of stockholders. At the peak of the prosperous twenties L. H. Sloan of Standard Statistics wrote:

> For a time at least even when earnings are low or nil, interest and current dividend obligations will be met out of surplus. There is ample basis for the belief that, in the past, the total payments annually to security owners has been one of the most stable elements in our economic structure.[17]

Along this same line, T. J. Kreps in a study of dividend disbursements and interest payments from 1929–32 concludes that a substantial portion of the interest and dividend payments came from surplus.[18]

Dr. E. R. A. Seligman, former president of the American Economic Association, has written that if corporations "set aside nothing for reserves and then have a succession of bad years they may be forced into bankruptcy."[19]

Noel Sargent, representing the National Association of Manufacturers, made the following statement in testimony before the United States Senate Committee on Finance on May 7, 1936:

> Largely because of the existence of corporate surpluses it has been possible to maintain dividend payments in many companies during a period when earnings were not sufficient to permit such payments.[20]

Many other economists and businessmen testified before the Senate Finance Committee in 1936 in an effort to prevent passage of the Undistributed Profits Tax. A. A. Ballantine, repre-

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[17] L. H. Sloan, *Corporation Profits* (New York: Harper & Brothers, 1929), p. 265.

[18] T. J. Kreps, "Dividends, Interest, Profits, Wages, 1922–35," *Quarterly Journal of Economics*, August, 1935, p. 573.

[19] E. R. A. Seligman, "Taxes on Surplus Called a Danger," *New York Times*, March 22, 1936, Section 3, pp. 1, 6.

[20] Testimony of Noel Sargent, Hearings Before Finance Committee, *op. cit.*, p. 659.

senting the Merchants Association of New York, presented figures showing that all business during the five years 1930–34 paid out $26,500,000,000 more than was produced by those businesses.[21] Mr. James Emery, General Counsel of the National Association of Manufacturers, said: "The facts demonstrate that corporate dividend payments over the past fourteen years are substantially 25 per cent in excess of earnings, and this has been particularly true in the field of manufacture."[22]

Solomon Fabricant of the National Bureau of Economic Research has directed extensive research delving into corporate earnings and savings, most of the investigation being based upon income tax data. From these aggregate figures Mr. Fabricant writes the following conclusion:

> During the post-War period a substantial portion of earnings (after taxes) was retained in the form of corporate savings. For the eight years, 1922–1929, these savings amounted to 32 per cent of net income after the deduction of income taxes. But the crash changed the situation completely, and by the end of 1932 accumulations of more than a decade had been drawn upon to sustain at least partially the income of stockholders. During only three years, 1930, 1931, and 1932, the profits saved in the preceding ten years were disbursed. Fortunate indeed were those with such a reserve upon which to draw.

A footnote qualifies the above statement:

> These figures refer to the aggregate of all corporations. If the large corporations in which dividends constitute the chief means of distributing earnings were considered separately the reduction of surplus would not be so marked.[23]

Joseph P. Kennedy in a feature article in *The Saturday Evening Post* extols the virtue of corporations in providing a reserve against the inevitable rainy day and points out that millions of people have become investors in securities and count upon continuity of their dividend returns in budgeting their living expenses.[24] Has the rainy day reserve to which Mr.

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[21] *Ibid.*, testimony of A. A. Ballantine, p. 422.

[22] *Ibid.*, testimony of James Emery, p. 682.

[23] S. Fabricant, *Recent Corporate Profits in the United States* (New York: National Bureau of Economic Research, April 18, 1934), Bulletin No. 50, pp. 10–11.

[24] J. P. Kennedy, "Big Business, What Now?," *The Saturday Evening Post*, June 16, 1937, p. 80.

Kennedy refers provided "continuity of dividend returns" and "the continuous flow of dividends"?

It is customary for standard texts to mention the advisability of creating a surplus in order to pay dividends in lean years. For example, page 594 of *The Financial Handbook* says:

> In most corporations it is expected that earnings will fluctuate. The regularization of dividends recommended above may be accomplished in the face of fluctuating earnings by paying out of the profits of prosperous years only a portion of the earnings, reserving the remainder in a dividend reserve or in a surplus account. This may be drawn upon for dividends in lean years.[25]

Again on page 581 of the *Handbook* is the following:

> Intermittent dividends, dependent upon the amount and frequency of net earnings may be distributed; or the directors may retain in earned surplus an amount sufficient to regularize dividends in spite of fluctuations of net earnings.

Every stockholder should know by this time that dividends do not come from surplus and that directors may retain in earned surplus an amount sufficient to regularize dividends and still not pay any dividends when earnings decline.

From accounting texts come the following statements:

> The total amount of earned surplus is available for dividend declaration but sound business policy dictates that a reasonable portion of the profits of each year be retained in the Company for the following reasons . . . To provide funds out of which dividends may be paid in years when losses are sustained or the profits are small.[26]
>
> A surplus should be accumulated to meet unexpected losses and for other unseen contingencies. When this is done, if it seems wise, this surplus may be drawn upon to pay dividends in poor years when the profits are not sufficient for that purpose, and in this way dividends be equalized.[27]

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[25] R. H. Montgomery, *The Financial Handbook* (New York: The Ronald Press, 1937).

[26] R. L. Mannix, *Accounting for Corporations* (Boston: Insurance Press, Inc., 1934), p. 122.

[27] R. J. Bennett, *Corporation Accounting* (The Ronald Press, 1920), p. 134.

Corporations that are conservatively managed prefer to retain all earnings over the amount of reasonable dividends as a fund that will be available in case of economic depression or unforeseen contingencies.[28]

In the management of Surplus, it is not the usual policy to distribute the entire amount available. Rather some should be retained in the business until at least a sufficiently large amount has been stored up to assure a fairly regular continuance of dividends during periods of poor business as well as when business is prosperous.[29]

Just how does the retention of earnings in a profitable year provide a "*fund* that will be available in case of economic depression," or a "*fund* out of which dividends may be paid in years when losses are sustained," or a "*surplus* which may be drawn upon to pay dividends in poor years," and how is it that a corporate surplus may be "*stored up* to assure a fairly regular continuance of dividends during periods of poor business"?

Typical of the statistical data frequently presented to show the effectiveness of corporate reserves is the following excerpt from an article by G. H. Sage.

NECESSITY OF FINANCIAL RESERVES

The building up of adequate financial reserves, therefore, through the prosperous years for use in depression years as rainy day reserves, appears not merely desirable but in fact essential. In this connection the experience of American industry over the past decade and a half, especially in the last few years of the depression, is exceedingly revealing. From official treasury figures it appears that during the prosperous period 1922–1929 earnings generally increased; only part of them however, were distributed in the form of dividends, the balance being retained in the business. In the period 1930–1933, however, although earnings changed into substantial losses, dividends continued to be paid out of the surplus previously accumulated from undistributed earnings. For the 13 year period, in fact, dividends aggregated $50,700,000,000 as against $41,000,000,000 of final net income. Moreover, for the period 1930–1934 the disbursements of corporations exceeded receipts by $26,600,000,000, all, it is to be noted, from so-called rainy-day reserves.[30]

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[28] J. O. McKinsey and H. S. Noble, *Accounting Principles* (South-Western Publishing Company, 1935), p. 454.

[29] R. B. Kester, *Principles of Accounting* (The Ronald Press, 1939), p. 468.

[30] G. H. Sage, "Dividend Policy and Business Contingencies," *Harvard Business Review*, Winter, 1937, p. 251.

The fallacy of such reasoning is easily demonstrated. Suppose only fifteen companies made reports to the treasury department over the period 1922–33. Before 1930 let us say each company retained one-half the total net income thereby creating rainy day reserves. It is entirely possible and reasonable to assume a 1930–33 record somewhat as follows:

| | |
|---|---|
| Net Income of Five Companies, 1930–33 | $10,000,000 |
| Dividends Paid by These Companies, 1930–33 | 9,000,000 |
| Earnings Retained by Five Profitable Companies | $ 1,000,000 |
| Net Loss of Ten Companies, 1930–33 | 5,000,000 |
| Dividends Paid by These Companies, 1930–33 | –0– |
| Dividends Paid from Surplus, Fifteen Companies Combined | $ 4,000,000 |

So far as official treasury figures are concerned, we could say the net income was $5,000,000, dividends of $9,000,000 were paid, and $4,000,000 came from earnings retained in the twenties.

That surplus reserves do not insure corporate financial stability is hardly to be questioned, and there is considerable evidence that reinvestment of earnings may be made at the stockholder's expense. From time to time various writers have suggested that earnings should be distributed in large measure in the year earned regardless of the surplus situation, and that when funds are needed in the enterprise new capital should be secured through the issue of rights or through the regular capital markets. The 1936 Revenue Act taxing undistributed profits was specifically in line with this doctrine.[81]

[81] George C. Haas, treasury expert testifying before the Committee on Finance, United States Senate, in 1936 said:

"It is argued by some that stockholders may be reluctant or even unwilling to reinvest in any given enterprise any large fraction of the earnings distributed to them in dividends. But this argument assumes that corporate management may justly reinvest earnings in a particular enterprise against the desire of the stockholders. In the last analysis, however, the earnings of a corporation belong to its stockholders; and stockholders are entitled to exercise a choice, which, under the present corporate practices they do not always possess, with respect to the disposition of these earnings. In so far as one effect of the proposed change will be to encourage corporate managements to obtain the consent of their stockholders for capital expansion, and to give to stockholders, the real owners of the corporation, a greater control over the disposition of their earnings, this effect is altogether desirable."

Rexford G. Tugwell, prominent in the early days of the New Deal, deplores the disturbing effects of corporate savings as contributing toward business fluctuations. He refers to the inexpert self-allocation of capital and explains that corporate surpluses are converted into industrial equipment by individual businesses without any general check on the likelihood of efficiency in use. Such a system in his opinion results in overequipped and overexpanded companies and industries in some cases, while other concerns and industries starve for lack of capital.[32]

It should not be inferred by any means that government officials are the only ones that believe stockholders or the investment market should direct the flow of earnings, savings, or new capital into industry. In his article "Depreciation and Savings," published in *The Accounting Review*, H. G. Kimball objects to withholding from the investor amounts charged to depreciation and not invested in plant assets during the fiscal year. He maintains that such action is harmful and results in dissipation of savings instead of their preservation.[33]

The *Financial Handbook* voices some doubt concerning the policies of income administration followed in the past and points out that large surpluses create investment problems, that bigness is an obsession of American business, and that present evidence of tremendous excess of productive capacity in certain lines of industry indicates unwise expansion.[34]

Just prior to 1920 corporate enterprises had made a tremendous amount of war profits. David Friday estimates that not more than one-fourth and probably not more than one-fifth of that profit ever was actually received by the stockholders.[35] Means and Ware, in *The Modern Economy in Action*, question the efficacy of corporate management in administering the earnings and suggest that the investors' interest is almost as completely at the mercy of the corporate control as is that of the

[32] R. G. Tugwell, *The Industrial Discipline* (New York: Columbia University Press, 1933), pp. 203–27.

[33] H. G. Kimball, "Depreciation and Savings," *The Accounting Review*, December, 1935, pp. 365–69.

[34] Montgomery, *op. cit.*, p. 595.

[35] D. Friday, *Profits, Wages, Prices* (New York: Harcourt, Brace & Company, 1921), p. 68.

worker. They emphasize the fact that state laws which once limited the things which the directors of corporations could do with their stockholders' money have been liberalized, since states compete with one another for the lucrative business of chartering corporations and collecting from them taxes and fees.

> In this situation, many stockholders have found that their board of directors is most adept at keeping the company's earnings from reaching them. Many and various devices are familiar to the student of corporate practices and to the stockholder who wonders what has happened to his expected dividends and to the market value of his stock. Large salaries may be paid to both necessary and superfluous officers—to the ever-convenient battery of vice-presidents, for instance; contracts for services, or for the purchase of supplies at exorbitant prices, may be given to companies in which directors have large interests; fifty-seven different varieties of stock issues may be brought out, each so complicated that the ordinary stockholder could not possibly be expected to understand the rights to which he was or was not entitled.[86]

Graham and Dodd in examining the investor's interests in corporate profits and surplus are equally dissatisfied with common practices, and contend that stockholders are entitled to receive the earnings on their capital except to the extent they decide to reinvest in the business, and that management should retain or reinvest earnings only with the specific approval of the stockholders.

> If it should become the standard policy to disburse the major portion of each year's earnings (as is done abroad), then the rate of dividend will vary with business conditions. This would apparently introduce an added factor of instability into stock values. But the objection to the present practice is that it *fails* to produce the stable dividend rate which is its avowed purpose and the justification for the sacrifice it imposes. Hence instead of a dependable dividend which mitigates the uncertainty of earnings we have a frequently arbitrary and unaccountable dividend policy which aggravates the earnings hazard. . . .In the end such fluctuations will work out more to his advantage than the present method of attempting, usually unsuccessfully, to stabilize the dividend by large additions to the surplus account.[87]

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[86] G. C. Means and C. F. Ware, *The Modern Economy in Action* (New York: Harcourt, Brace & Company, 1936), pp. 50–51.

[87] B. Graham and D. L. Dodd, *Security Analysis* (New York: McGraw-Hill Book Company, 1934), pp. 334–35.

The mere retention of earnings during periods of prosperity does not assure dividends at a later date, especially during years when the business operates at a loss. There are many who insist that retention of earnings from a profitable year may have little if any influence upon ability to pay dividends at any later time. That it is advantageous to stockholders if a large portion of earnings is retained in the business rests upon two assumptions. The basic premise assumes that whatever benefits the company is immediately of advantage to the stockholder. The conclusion that stockholders benefit when earnings are retained follows logically from the assumptions, but whether it is more advantageous to reinvest than to receive a cash dividend is a distinctly different proposition. Earnings withheld for corporate purposes naturally strengthen the company temporarily. Whether the action proves profitable to the stockholder depends upon subsequent events generally and timely action of the individual stockholder in selling his stock.

Even if we do not question the right of management to reinvest earnings without consideration of the stockholders' opinions, we find no agreement that the surplus thus created is any panacea for depressions or that dividends are maintained during slack periods because of surplus accumulations. Figures compiled from *Statistics of Income* and used to show that $26,500,000,000 more was paid out than produced during the 1930–34 slump are interpreted in a very different light by members of the United States Treasury Department. These officials show that depression dividends, wages, and other payments came out of current receipts and not from accumulated liquid surpluses.[38]

Don D. Humphrey shows that the *Statistics of Income* figures are misleading when used to prove that dividends and wages were paid from surplus during the depression years.[39] Albert Hubschman suggests that under present-day mass production technique sales are made before manufacture proceeds very far, that rainy day reserves are therefore unnecessary, and that wages and dividends paid during the depression did not exceed the current cash receipts.[40]

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[38] Testimony of George C. Haas, Hearings Before Finance Committee, *op. cit.*, pp. 59–60.

[39] Humphrey, *op. cit.*, pp. 223–34.

[40] Testimony of Albert Hubschman, Hearings Before Finance Committee, *op. cit.*

*The Nature of Surplus*

It would seem that a discussion of the nature of corporate surplus with its long standing position in law and finance is uncalled for, but it is quite apparent that ideas as to the functions and significance of corporate surplus are conflicting and somewhat confused. When it is affirmed that to the average citizen surplus means an excess of liquid funds over and above business requirements, one can be pardoned for some degree of dismay.

During the hearings before the Senate Committee on Finance pending passage of the 1936 Revenue Act, Senator Bailey wanted to know the amount of capital write-downs from 1931 through 1933. The figure disclosed was some $15,000,000,000, and that stupendous sum prompted the following discussion:[41]

> *Senator Bailey*: They could not remain solvent after the write-down, except for the fact that they made the write-down out of accumulated surplus. You could not write it out of capital structure; you have to write it out of surplus.
>
> *Mr. Haas*: You can write the capital down as well as the other.
>
> *Senator Bailey*: No. If you write-down the capital of a corporation, it becomes insolvent, and anybody can close it up. That is statutory. That is not a question of fact; that is a question of law. . . . Now, this write-down occurred without impairing the capital or making the corporations insolvent, and therefore they continued to operate. Suppose they had had no surplus, then the write-down would have broken every one of them and you would have this country filled with receiverships.
>
> *Mr. Haas*: Whether they can withstand the situation that you pointed out is largely contingent upon the nature of their assets.
>
> *Senator Bailey*: Just tell me how they would have withstood the write-down of $11,000,000,000 in three years if they did not have a surplus to be able to write it down. They would have certainly become insolvent. It kept millions of people employed, it kept the industries going and they employed the labor.
>
> *Mr. Haas*: No; I do not think so.

If one wishes proof to support the position taken by Mr. Haas it may be found in a study made by R. P. Marple in which he shows that legal capital has been used to absorb all sorts of losses and asset write-downs.[42]

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[41] Hearings Before Finance Committee, *op. cit.*, pp. 61–62.

[42] R. P. Marple, *Capital Surplus and Corporate Net Worth* (New York: The Ronald Press, 1936), pp. 96–97.

To those at all familiar with corporate finance and accounting technique it is well understood that surplus is simply a part of the stock equity and measures a cross section of all the assets of every kind. This much is certain: The surplus does not represent a cash fund; there is no way to look at the surplus figure and gain any notion as to what assets it may represent; and there is little direct relation between financial ability to pay dividends and amount of the surplus balance.

A few recognized authorities have made it clear that dividends in excess of current income may not be extensive, as suggested by the paragraph below:

> The limited significance of surplus in relation to dividend disbursements requires emphasis, particularly in view of certain common misconceptions. Dividends are *appropriated* from surplus but are paid (as a rule) in cash. Surplus is the yardstick or gauge which shows the amount of dividends which may be declared without impinging upon capital, but is not in itself a medium of disbursement. Surplus, moreover, is in general supported by a cross-section of all the assets, rather than by a fund of cash or other liquid resources. This means that surplus accumulation as a reservoir for dividends in lean years does not actually insure the ability to maintain the stream of payments to stockholders. In fact dividends can seldom be long continued in the absence of current profits, no matter how large the surplus account.[48]

*Dependence of Dividend Payments upon Current Revenue*

Earnings are retained when business is good. At such times corporate managers would be indeed pessimistic "kill-joys" if they could not see opportunities for a greater volume of business. Easier credit terms resulting in more accounts receivable and larger inventories are usually incidents of increased volume. With increased volume a realized fact, production methods and plant facilities need attention in the form of capital expenditures. As long as revenue volume is maintained at profitable prices the reinvested earnings pay dividends, but poor years and depression periods invariably make an uninvited and unwelcome, if not unexpected, appearance. The corporate managers may be wise to retain a portion of profitable year earnings for

[48] W. A. Paton, *Essentials of Accounting* (New York: The Macmillan Company, 1938), pp. 695–96.

purposes of increased business volume and to provide for future contingencies, but they do not and cannot set the earnings aside in some hoarded fund of cash or other liquid assets and cautiously await lean years when the fund will be utilized to pay dividends.

When the lean years come, sales volume drops off, profit margins disappear, collections slow down, and payables must be met. The retained earnings are invested primarily in inventories, receivables, and plant facilities—the *fund* or *reserve* to which we frequently refer. Receivables and inventories can be liquidated (probably at a loss), but the cash is not necessarily available for dividends. The business is geared to increased volume of production and must operate at reasonable capacity to be profitable. Working capital may be excessive at the moment of depression, but corporate management must conserve the cash in order to start production at the first signs of possible profitable operations on an increased scale. To pay dividends from liquidated inventories and receivables would be tantamount to borrowing money to pay dividends in the face of declining production, falling prices, and a discouraging immediate future outlook. Plant facilities built up during periods of profitable operation (thereby representing a major part of the surplus) usually prove excessive during slack periods of unprofitable operation. It is entirely possible to liquidate the surplus thus invested in plant capacity, inventories, and receivables, and the funds may be used for cash dividends, but this process of drawing upon reserves is wholly dependent upon continued sales and collections at *prices below costs* and is exactly what managers and stockholders seek to avoid. This process of disinvesting throws labor out of employment, is devastating to the market value of the stockholder's investment, and cannot be regarded as a satisfactory dividend reservoir.

Retained earnings need not be invested in the corporation at all, as many corporate managers could testify. Furthermore, a backlog of cash and liquid securities can be built up to provide dividends during depressions, but this procedure is wasteful and inexpedient and has not been followed extensively in practice. To create a reserve of idle cash funds is entirely foreign to American business psychology. In effect, corporate managers

would be saying: "We are operating profitably just now, but there may be danger ahead and we are afraid to expand the business. Therefore, we will keep part of the profits made this year, increase our bank account, and when times get bad you will be happy to receive a dividend check." The stockholder would undoubtedly be pleased to have a dividend check during poor years, but it might require considerable managerial courage to deplete the cash balance in periods of slack business when every kind of enterprise sets a premium on liquid reserves. It is very doubtful that investing retained earnings in government and municipal bonds would prove effective as a source of liquid funds in periods of general depression. If followed as a popular corporate practice, the securities would be dear during the upswing, and when needed, the market would be composed of many sellers and few buyers, thus forcing the corporation to buy at high prices and sell at low prices.

Retained earnings can be reinvested in business enterprises of a diverse nature, thus stabilizing income and distributing business risk. This holding of common stocks of other companies has been popular corporate practice, especially since the early twenties. It is obvious, however, that funds invested in equity securities are not available for corporate purposes during a severe depression.

Income once reinvested is exactly like all other corporate capital. If a stockholder buys one share of common stock in a company just beginning to operate, paying $100 therefor, he has provided $100 of the corporate capital. If at the end of three years total income of $50 per share has been earned and no dividends paid, the stockholder has contributed $150 of the total corporate capital. If total income had been paid to stockholders and additional stock sold, would the corporation be any less able to continue dividends? If bonds were issued to provide the additional capital, would capacity to pay dividends in the future be any different aside from the degree of caution necessary with considerable bonded debt in the capital structure? From whatever source the capital may come, it is amalgamated into a business enterprise and distribution of future income to equityholders is dependent entirely upon total income to be earned in the future. There is nothing sacred about the

dollars paid originally to create the corporation. Original dollars, reinvested earnings, and funds from new issues are exactly alike. Corporation law has placed a legal fiction around the formal stated capital on the assumption that creditors might be injured if this capital were paid to stockholders. If original capital is invested in a business which proves to be profitable, income can then be distributed, but if the enterprise is unprofitable, the original investment is lost. Income reinvested is exactly like the original capital in this respect and when losses occur, capital is impaired regardless of the legal fiction. Likewise, whenever dividends are paid there is a liquidation of corporate assets and a reduction in the common stock equity, and this liquidation of assets (aside from legal provisions) can be made as effectively from original capital as from surplus.

It is pertinent to remember that corporate ownership changes hands on the ticker tape and prices reflect the income retained as well as dividends paid. From the point of view of recent stockholders, reinvested earnings are part and parcel of the original capital and it would be senseless to assume future dividends would be paid just because a considerable portion of the price paid for the stock represents capitalized retained earnings.

*Possible Benefits of Retaining Earnings*

A word of caution is needed, not to qualify any of the statements made in relation to retaining earnings to pay future dividends, but to reiterate the writer's point of view. Earnings retained during the twenties by companies included in this study were not paid to stockholders to any appreciable extent during the poor years of the early thirties. It does not follow that reinvestment of earnings is to be deplored or that it is vicious practice and robs the common stockholder of his income. Earnings retained may result in much greater distribution of income to the stockholder *during the profitable periods* and market appreciation may be very attractive as a consequence. However, depression periods always come and it is wholly fallacious in theory as well as in practice to say that dividends withheld in the good years can or will be distributed in the bad years,

and many of the statistical studies purporting to show the stupendous amount of depression dividends which came from earnings retained through the twenties are misleading to say the least.

In this connection, it is recognized that any dividends at all in excess of current income must be declared from surplus created by reinvesting income of previous years or from surplus arising in some manner. A dividend cut of 80 per cent or more during the unprofitable years may therefore be a surprisingly modest reduction from the managerial point of view. The entire amount of dividends may very well be *declared* from *surplus* even though the funds to make payment may come from revenue of the period in excess of expenditures but less than the total cost of operation. In other words, surplus is likely to be invested in receivables, inventory, and plant assets to a considerable degree. This is not a "fund" or "reserve" which can be drawn upon directly for dividends, but output can be produced and sold during the poorest years if prices are reduced sufficiently. Sales below total cost of production liquidate the assets and consequently absorb the surplus. By this indirect method surplus is used to pay dividends during poor years, but to refer to the process as drawing upon a fund set aside for the purpose is unrealistic. We thus arrive at the anomaly that liquidation of large inventories and huge plant investments is not only the means of meeting operating deficiencies but is largely responsible for the losses in the first place.

There is no intention to minimize the extent of dividends paid through the most unfavorable period of business history and it is granted that even smaller amounts of depression dividends might have been paid had the companies retained little of the 1922–30 income. On the other hand, excess capacity of the corporations might have been much less and the depression of the thirties less severe if a more liberal dividend policy had been followed through the profitable twenties.

## *Objectives of the Present Investigation*

The previous discussion introduces some aspects of income administration. It is evident that differences of opinion exist in

regard to who should have the right to declare dividends and who should decide how much should be paid; as to relative merits of paying out or retaining a major portion of the annual net income; as to how the retained earnings should be invested; and as to the advantages of having a corporate surplus. It is easy to deduce forcible arguments to answer these questions and able scholars have expounded various angles at great length, though supporting some theory in part perhaps due to personal interests or prejudices.

Never since the days of ancient Egypt has so much thought been given to reserves and to savings in years of plenty in order to provide for the "Seven Lean Years." The federal social security program providing for the most gigantic reserves ever assembled has produced a flood of comment and speculation on what reserves can be expected to do and where the limits may be anticipated. The "ever normal granary" for agricultural crops is another phase of the reserve idea of saving in good years in order to supply needs created by bad years. American corporations have for decades been committed to the theory of reserves and have proceeded to create huge surplus balances. The Revenue Act of 1936 taxing undistributed profits provoked mostly protests and criticism from economists and managers of business enterprises who prophesied dire consequences if corporations are not permitted free rein in building up surplus reserves. Are corporate surpluses, social security reserves, and agricultural surpluses similar in nature?

Most studies of corporate profits have been made from the managerial point of view or from a broad social economic point of view, but a corporate enterprise exists only because a group of investors pool their resources and create the invisible, intangible, artificial being with neither a "body to be kicked nor a soul to be damned." This investigation is made, therefore, from the point of view of the small investor who may have a few shares of common stock in a very large corporation.

During the stirring industrial activity of the twenties there was great corporate growth and expansion, financed by issuing new securities and by reinvesting profits. Within limits of the sample the relative expansion from the two sources is shown, with ample evidence to suggest that retention of earnings may easily have led to overexpansion of productive capacity.

The present investigation presents concise evidence on what financial policies have actually been practiced in the operation of prominent, generally profitable, and widely owned American corporations engaged chiefly in the manufacture and distribution of basic commodities from 1922 through 1936. During these years of prosperity and depression there was ample opportunity to retain a part of abundant earnings and to create extensive surplus reserves. For several years after 1930, many and perhaps most business organizations had sufficient demands made upon reserves to test their efficacy in meeting financial reverses and stormy weather. It seems highly pertinent in this connection to know just how much a number of large corporations have earned, what portion of the income was paid in dividends, and what percentage of the total income was retained in the business. The year to year aggregates of an industry have little bearing on the problem. The vital issue to the investor is how much he receives in cash dividends from a specific company year after year, how much of the amount available for dividends is withheld without his active voice in the matter, and how the retained portion is invested. The amount of net income reported to the stockholder is not the end of the problem, however. Profits and losses entered directly in the surplus and reserve accounts may be just as potent in providing or dissipating funds available for dividends as items reported as expense or revenue. Reserves provided for contingencies, accidents, insurance, foreign exchange fluctuations, and other possible events represent net assets and net worth earmarked (after a fashion) to absorb the shock of a possible event, and if the events never occur, the reserves represent earnings, pure and simple.

The heart of the controversy over policies of income administration is whether or not earnings of profitable years can be reinvested and drawn upon to pay dividends in depression periods. This study presents a fifteen year record of well known corporations and shows the extent to which regular common dividends were paid by these individual companies during periods of profitable operation and through the severe depression and indicates the degree of causal relationship between cash dividends paid in poor years and the percentage of earnings retained in the good years.

In a study of corporate savings it is of vital interest to know what becomes of earnings that are retained. In Chapter 4 income sheet and balance sheet data of each company are summarized for each phase of the cycle and the uses to which retained earnings were put are emphasized. Of equal significance is the liquidation of assets when companies operate at a loss, because the entire validity of surplus reserves must be determined at this point.

When corporate directors elect to withhold earnings in a given period, a surplus balance results. In the process of profitable operation, revenue and income exceed costs of production. Assets which measure the volume of income and revenue therefore exceed costs of production plus distributions to investors, and represent the surplus increase. In unprofitable years losses are charged to surplus as a balancing entry, but when costs exceed revenue the deficiency must be met from asset liquidation of some description or new equities must provide the needed funds. Year after year the changes in asset categories are measured and related to profits or losses. For a fair cross section of industry we have explicit data showing what portion of retained earnings went into working capital, what percentage was utilized for plant expansion, what fraction was used to retire debt, and, in short, what became of the surplus in specific instances as well as in aggregates for an industry or group of companies. This treatment throws considerable light on the process of providing liquid funds to pay for actual disbursements when revenue is insufficient to meet expenses or expenditures.

Many incidental problems are connected with the broad study of corporate income administration, but the central theme and thesis of the material presented in this study is to show by specific companies the earning and dividend records during the prosperous twenties and to demonstrate that a very small portion of dividends withheld during the good years reached the stockholder during poor years. Seventy-two specific examples are analyzed to show how the surplus was invested when profits were retained and to show the process of asset liquidation during the period of severe operating losses. In the past, have corporations been able to use the rainy day reserves effectively, and, if so, what form or type of investment proved most satisfactory?

If a corporation can live off its surplus fat when the need arises, does it make any difference what part of the anatomy is fattest?

*Source of Data*

Reports to stockholders are the primary source of information available to the general public concerning corporate affairs. No matter how deficient the financial statements may be, the individual investor relies directly or indirectly upon this information for his investment analysis. In an analysis of corporate earnings and how they are utilized, viewed from the position of one of the eleven million ordinary citizens who own the corporations, it is logical to base the investigation upon data taken from reports to stockholders.

In the library of the School of Business Administration at the University of Michigan there are reports to stockholders of more than five hundred American corporations including railroads, banks, public utilities, insurance companies, and industrial enterprises of all sizes operating in all parts of the United States. These reports to stockholders provide the raw material for the present investigation.

*Companies Selected and Period Covered*

A sample of companies is desired which will enable us to measure corporate earnings over a considerable period of time and through at least one complete business cycle. Industrial enterprises provide the best examples of very rapid self-financed growth, huge amounts of reported profits and scanty cash dividends, large surplus balances, great excess productive capacity, and companies which attract the investor to make speculative commitments. We desire to know how profitable these companies have been and to observe their policies of income administration in view of all the business events over a period of time long enough for most economic forces to be reflected in the operating reports.

Transportation, public utility, finance, mining, and oil companies are eliminated because these industries are subject to varying degrees of governmental control and regulation or have peculiar problems of depreciation and depletion accounting. In addition, the capital structure of transportation and public utility companies consists of bonds and preferred stocks to a

great extent, and we are more interested in income administration from the point of view of the common stockholder in companies where common stock owns much of the total invested assets.

A considerable number of reporting companies published income sheets or balance sheets or both which proved to be too condensed for analysis, and in other cases the net income reported minus dividends paid does not by any means agree with changes in balance sheet surplus. The essence of a study of retained earnings is to determine what becomes of the surplus, hence in those cases where there was totally inadequate information and no hint at a surplus analysis it was necessary to eliminate the company from the sample. Some corporations which published adequate reports in the early twenties were absorbed by other firms, were liquidated, or otherwise disappeared from the business scene. A few companies were reorganized one or more times during the period and in the process went through so many contortions of revaluing assets and substituting new equities for old that the amount of retained earnings became completely obscured, and of course these companies could not be included in the sample.

During the war and immediately thereafter earnings and financial policies were influenced predominately by war activities and it would seem of little value to go into that period to study corporate profits. The postwar correction of 1921 brought about severe declines in inventory values, liquidation of receivables, and a return to more stable price levels in general. The balance sheets of 1921 reflect the new price levels which remained unusually stable through 1930, thus providing an admirable condition for the study of earnings and their uses. If we include the fifteen years 1922–36 the period covers a decade of prosperity, the collapse during the early thirties, and a period of recovery after 1933.

### *Characteristics of the Sample*

After eliminating companies which did not operate throughout the period, those reorganized beyond recognition, and those which reported entirely inadequate information, reports to

stockholders of seventy-two well known corporations engaged in twelve distinct lines of industrial activity were available for study.

The writer is well aware of the biased nature of the sample when compared to all corporations. Any company which remained in business from 1921 through 1936 and published reports to stockholders (certified in most instances by leading accounting firms) must have been profitable or else very strong at the beginning of the period. The peculiar concern of this study, however, is to discover what has been done with corporate earnings over a long period of time in the larger and generally more profitable concerns where the small stockholder has little voice in the matter. If some of the companies were unprofitable throughout the period, so much the better. How can an unprofitable enterprise survive for fifteen years? Analysis of the reports from unprofitable concerns helps to explain the process of liquidating assets in order to meet losses.

Within limits of reports available, every effort was made to secure a representative number of corporations engaged in several distinctly different types of industrial enterprise in order to determine whether companies in one kind of business activity administer income in a fashion characteristic and peculiar to the industry. Much has been said about overexpansion of plant facilities in the manufacture of heavy equipment and capital goods such as railway equipment, machine tools, iron and steel, agricultural equipment, rubber, and automobiles. It should prove interesting to see how the prominent companies in these industries financed plant expansion and if it was accomplished from reinvested earnings the implications would seem very significant, especially in relation to an undistributed profits tax. A large commitment in plant assets appears essential to the manufacture of capital goods regardless of the source of investment. Companies engaged in mercantile and trading activity, in the manufacture and sale of tobacco and beverages, and in food processing, must have an asset structure greatly different from companies engaged in capital goods manufacture. Much of their capacity to produce profits evidently comes from advertising campaigns, trade-marks, and brand names, and consequent good will, while a substantial portion of the total assets must be represented by receivables and inventory.

*Adequacy of the Sample*

Names of the seventy-two companies included in the sample are presented in Appendix I in order to show the wide range of industrial activity represented and the size of enterprises selected.

In order to draw conclusions and to generalize, it is important to know how much of each industry is included in the sample analyzed. Standard Statistics Company publishes a classified bi-weekly survey analyzing investment possibilities in most companies of market significance.[44] This list appears to be an ideal device to test the selected sample, since it includes practically all companies worthy of investment consideration on a wide scale, but does not include those which are closely held and of a semiprivate enterprise nature. The Standard Statistics list was examined as of July 7, 1937, and compared with the selected sample. Gross assets of each company not included in the study were tabulated from Standard Statistics for the year 1936, while the 1921 year end figures were obtained from Moody's Industrial Volume of 1922.

In Table 2 assets of seventy-two companies included in the twelve industries are combined in order to show the size and significance of the sample. With seventy-two companies engaged in twelve distinct lines of business activity employing in the neighborhood of ten billion dollars of invested assets, there should be adequate opportunity to determine how depression dividends were paid and how the surplus was used. The percentages in Table 2, it should be made clear, represent the fraction of assets owned by companies included in this study compared to the total assets invested by all important companies which engaged in each industry during all of the fifteen years examined. In all industries except automobile equipment manufacture and retail trade, the companies examined comprise over 60 per cent of all assets invested in the industry by important corporations which operated during the 1922–36 period. Companies which constitute the retail trade sample are fairly representative and comprise almost one-half of the industry. The

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[44] Standard Trade and Securities, *Basic Survey* (New York: Standard Statistics Company, Inc.), Volume 85, No. 2, Section 2, July 7, 1937.

most unsatisfactory sample of all, automobile equipment, has little to recommend it except the totally random nature of selection. If the industry is peculiar in regard to its dividend policy or if retained earnings were invested in some unusual manner by manufacturers of automobile supplies even the limited sample should reveal the fact.

TABLE 2—GROSS ASSETS OF COMPANIES INCLUDED IN SAMPLE, CLASSIFIED BY INDUSTRY, 1921 AND 1936
(Amounts in thousands of dollars)

| Industry | 1921 | | 1936 | |
|---|---|---|---|---|
| | Amount | Per Cent of Industry Total* | Amount | Per Cent of Industry Total* |
| Railway equipment | $ 357,990 | 63.43 | $ 279,933 | 61.08 |
| Machinery manufacturing | 686,770 | 68.25 | 921,853 | 69.50 |
| Electrical equipment | 504,080 | 98.78 | 582,604 | 98.58 |
| Tire and rubber | 641,750 | 91.68 | 654,501 | 94.81 |
| Iron and steel | 3,079,918 | 81.48 | 3,262,238 | 80.40 |
| Automobile | 618,461 | 70.37 | 1,601,714 | 91.25 |
| Automobile equipment | 89,493 | 29.11 | 111,336 | 23.29 |
| Chemical producing | 691,449 | 61.86 | 1,288,518 | 86.27 |
| Metal container | 161,758 | 100.00 | 316,108 | 100.00 |
| Food processing | 435,993 | 65.05 | 569,407 | 59.47 |
| Retail merchandising | 400,548 | 51.56 | 749,167 | 45.11 |
| Tobacco and beverage | 548,583 | 81.72 | 758,584 | 87.89 |
| Total | $8,216,793 | | $11,095,963 | |

* This percentage expresses the relationship between gross assets of companies included in the sample and total gross assets of all important companies in the industry.

## *Surplus Reported by Companies Studied*

Reference has been made to the virtues of corporate surplus as a panacea for financial difficulties likely to arise during periods of depression, and excerpts were quoted some of which praised the creation of surplus while others ridiculed the idea. It may be interesting to observe the surplus figures reported by the seventy-two companies included in the study. Table 3 shows that the sample is large enough and that selected companies possess enough surplus to test thoroughly the effectiveness of surplus liquidation in meeting the difficulties brought about by the "rainy days."

In each industry surplus was greater in 1929 and 1930 at the end of the boom period than at the 1921 year end where the analysis begins. To some extent at least corporations were saving for some purpose and in most industries the surplus increase during the prosperity period was very material. In every industry surplus decreased during depression years. In aggregate, with from two to three billion dollars of surplus, the sample should prove entirely adequate to reveal any uses to which surplus can be put. Doubtless individual companies created much greater surplus reserves than others, and careful examination of the earnings record, dividends paid, and methods of investing the retained earnings by each of the seventy-two companies should throw considerable factual light on how the surplus reserves were relied upon during the poorest years.

**Table 3—Surplus of Companies Included in Sample, Classified by Industries, 1921–36**
(Amounts in thousands of dollars)

| Year | Industry: Railway Equipment | Machinery Manufacturing | Electrical Equipment | Tire and Rubber | Iron and Steel | Motor Cars | Automobile Equipment | Chemical | Metal Container | Food Processing | Retail Trade | Tobacco | All Groups |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1921 | $ 82,290 | $125,322 | $112,451 | $ 58,104 | $ 790,496 | $107,952 | $32,546 | $196,937 | $29,985 | $ 94,204 | $ 43,183 | $ 89,698 | $1,763,168 |
| 1922 | 87,134 | 118,931 | 121,721 | 71,810 | 795,581 | 143,845 | 37,918 | 174,351 | 35,174 | 67,226 | 41,011 | 80,776 | 1,775,478 |
| 1923 | 95,331 | 118,930 | 128,349 | 80,219 | 879,738 | 165,642 | 39,429 | 204,112 | 42,754 | 66,127 | 62,991 | 109,874 | 1,993,496 |
| 1924 | 97,413 | 138,927 | 123,561 | 104,835 | 907,233 | 138,611 | 45,027 | 217,728 | 48,932 | 65,101 | 87,077 | 144,163 | 2,118,608 |
| 1925 | 83,042 | 162,830 | 137,563 | 134,661 | 927,057 | 225,057 | 49,732 | 212,659 | 61,221 | 79,291 | 109,574 | 171,518 | 2,354,205 |
| 1926 | 106,587 | 189,684 | 157,285 | 130,841 | 1,008,461 | 203,380 | 56,321 | 241,632 | 46,891 | 96,401 | 156,344 | 197,259 | 2,591,086 |
| 1927 | 100,310 | 199,067 | 172,029 | 141,410 | 832,305 | 332,602 | 62,560 | 293,545 | 53,478 | 101,180 | 167,574 | 172,191 | 2,628,251 |
| 1928 | 93,616 | 160,569 | 199,764 | 113,167 | 864,029 | 472,159 | 67,308 | 330,384 | 61,351 | 117,436 | 207,410 | 201,227 | 2,888,420 |
| 1929 | 97,208 | 185,458 | 254,025 | 100,814 | 924,412 | 570,624 | 67,176 | 399,605 | 74,941 | 139,434 | 233,414 | 222,493 | 3,269,604 |
| 1930 | 50,552 | 197,691 | 261,346 | 59,103 | 943,249 | 498,068 | 65,728 | 472,449 | 85,897 | 149,625 | 232,818 | 256,359 | 3,272,885 |
| 1931 | 79,651 | 176,291 | 237,254 | 30,306 | 850,375 | 419,521 | 56,651 | 366,714 | 87,110 | 133,899 | 228,958 | 290,368 | 2,957,098 |
| 1932 | 58,674 | 130,814 | 170,277 | 7,236 | 712,399 | 326,611 | 47,275 | 332,551 | 84,899 | 115,344 | 188,467 | 310,906 | 2,485,453 |
| 1933 | 49,332 | 122,294 | 144,192 | 14,103 | 653,065 | 334,564 | 51,782 | 334,144 | 91,363 | 106,653 | 213,378 | 294,812 | 2,309,682 |
| 1934 | 41,459 | 118,715 | 137,960 | 16,722 | 353,566 | 344,347 | 53,322 | 353,290 | 89,010 | 102,824 | 230,355 | 280,491 | 2,389,915 |
| 1935 | 37,686 | 147,611 | 151,322 | 27,549 | 621,420 | 442,576 | 55,093 | 391,545 | 95,495 | 100,246 | 265,009 | 231,468 | 2,299,166 |
| 1936 | 37,157 | 179,111 | 167,031 | 51,744 | 347,473 | 493,521 | 57,553 | 401,599 | 97,534 | 101,010 | 274,312 | 229,283 | 2,437,328 |
| No. of companies | 6 | 11 | 2 | 4 | 7 | 7 | 5 | 7 | 2 | 8 | 6 | 7 | 72 |

## Chapter 2

# CORPORATE EXPANSION, 1922–30

### *Reinvested Earnings, 1922–30*

From the managerial point of view, total income is all income available for distribution to securityholders whether in the form of interest or dividends. It is sometimes suggested that income taxes represent a distribution of income to the government for its participation in the business enterprise, but total income is here defined as "Income after Taxes." Reports to stockholders for these companies were certified by prominent public accounting firms and it is fair to assume that reported figures are reasonable estimates of the actual accrued income, especially when the entire nine years are included in one period.

It is difficult to state categorically what constitutes retention of earnings in sizable proportions, but perhaps we can agree that 40 per cent or more of total income retained in the business for a decade constitutes a considerable degree of surplus accumulation. By the same arbitrary rule, we can say that retention of only 25 per cent or less means generous distribution of the income. Seventeen of the seventy-two sample companies (about 24 per cent) retained more than one-half their total income through the profitable years, and thirty companies (42 per cent of the enterprises) retained more than 40 per cent of their income. Fourteen companies (19 per cent of the sample) distributed to equityholders 75 per cent or more of the good year earnings and retained 25 per cent or less. Between these extremes are the companies which followed a middle-of-the-road course in reinvesting earnings. In summary:

14 companies, 19% of sample, retained less than 25% of income

28 companies, 39% of sample, retained 25% to 40% of income

30 companies, 42% of sample, retained more than 40% of income

Table 4 shows in more detail the extent to which earnings were retained during the prosperous twenties. Forty-six of the seventy-two companies (64 per cent) retained between 30 per cent and 55 per cent of total income during the good years.

TABLE 4—CLASSIFICATION OF COMPANIES BY PERCENTAGE OF TOTAL NET INCOME RETAINED, 1922–30

| Per Cent Retained | Number of Companies | Per Cent Retained | Number of Companies |
|---|---|---|---|
| Less than 5 | 2 | 45–49.9 | 5 |
| 5– 9.9 | 1 | 50–54.9 | 8 |
| 10–14.9 | 1 | 55–59.9 | 4 |
| 15–19.9 | 5 | 60–64.9 | 2 |
| 20–24.9 | 5 | 65–69.9 | 2 |
| 25–29.9 | 3 | 70–74.9 | -0- |
| 30–34.9 | 12 | 75–79.9 | -0- |
| 35–39.9 | 12 | 80–84.9 | -0- |
| 40–44.9 | 9 | 85–89.9 | 1 |

Table 5 displays by name thirty-one companies which retained much of their earnings, and fourteen corporations which paid generous dividends. In order to give some idea of the magnitude of earnings retained in nine profitable years, the total income retained is expressed as a percentage of net assets invested as of January 1, 1922. This percentage figure shows also the extent of expansion resulting from reinvested income during the prosperity period.[1]

It is interesting to observe that companies from the various industries are included in both groups, although retail merchandisers are prominent in the group retaining a high percentage of earnings. Those companies marked with an asterisk have more than $100,000,000 of invested assets. There is little indication that these large companies retain more or less of their income than companies of any other size. Of the twenty-seven *largest* companies, eight retained more than 40 per cent of prosperity period earnings and seven retained less than 25 per cent. Fourteen of the companies have less than $25,000,000 of assets invested. Seven of these retained over 40 per cent of their income and only one retained less than 25 per cent.

[1] In most cases the prosperity period ends with 1929 or 1930, but in a few instances the period extends through 1931. Major tobacco companies operated most profitably until 1933. *Net assets* is defined as total assets minus current liabilities.

TABLE 5—EXPANSION FROM RETAINED EARNINGS
Selected Companies, 1922–30

| Name of Company | Per Cent of Total Income Retained | Increase in Assets from Retained Earnings† |
|---|---|---|
| Thirty-One Companies that Retained a Large Fraction of Total Income | | |
| Spicer Manufacturing Corp. | 88 | 70 |
| Mullins Manufacturing Corp. | 65 | 57 |
| Hershey Chocolate Corp. | 68 | 121 |
| Sears, Roebuck & Co.* | 63 | 85 |
| J. C. Penney Co. | 60 | 371 |
| S. S. Kresge Co. | 59 | 228 |
| Chrysler Corp. | 59 | 117 |
| Firestone Tire & Rubber Co.* | 58 | 103 |
| Mathieson Alkali Works, Inc. | 55 | 75 |
| Deere & Co. | 53 | 37 |
| National Acme Co. | 53 | 5 |
| J. I. Case Co. | 52 | 43 |
| Borden Co.* | 50 | 104 |
| Continental Can Company, Inc. | 50 | 108 |
| Hart, Schaffner & Marx | 50 | 44 |
| F. W. Woolworth Co.* | 50 | 108 |
| Loose-Wiles Biscuit Co. | 49 | 39 |
| Otis Elevator Co. | 49 | 98 |
| May Department Stores Co. | 48 | 59 |
| Mack Trucks, Inc. | 47 | 87 |
| American Can Co.* | 46 | 51 |
| Nash-Kelvinator Corp. | 44 | 268 |
| International Harvester Co.* | 44 | 34 |
| Air Reduction Company, Inc. | 42 | 114 |
| Packard Motor Car Co. | 42 | 80 |
| Reo Motor Car Co. | 41 | 78 |
| Gulf States Steel Corp. | 41 | 16 |
| Allied Chemical & Dye Corp.* | 40 | 42 |
| Coca-Cola Co. | 40 | 117 |
| Timken Roller Bearing Co. | 40 | 207 |
| Fourteen Companies that Retained a Small Fraction of Total Income | | |
| American Tobacco Co.* | 24 | 41 |
| Consolidated Cigar Corp. | 24 | 91 |
| Allis-Chalmers Manufacturing Co. | 22 | 13 |
| Bethlehem Steel Co.* | 22 | 17 |
| Wheeling Steel Corp. | 22 | 13 |
| Baldwin Locomotive Works | 18 | 9 |
| Electric Storage Battery Co. | 18 | 27 |
| Worthington Pump & Machinery Corp. | 18 | 6 |
| National Biscuit Co.* | 17 | 30 |
| E. I. du Pont de Nemours & Co.* | 15 | 23 |
| Republic Steel Corp.* | 12 | 5 |
| Crucible Steel Company of America | 6 | 2 |
| American Locomotive Co. | --- | −18 |
| American Car and Foundry Co. | --- | −3 |

* Invested assets of $100,000,000 or more.
† 1922–30 retained earnings as a per cent of 1921 assets.

*Corporate Expansion*

Table 6 shows the importance of reinvested earnings as a means of financing corporate growth. Over 44 per cent of the companies grew from reinvested earnings entirely, while almost three-fourths of these manufacturers financed at least 50 per cent of their growth from within.[2] It is recognized, of course, that if a concern retains all of a scant income it is of little significance to say that 100 per cent of the expansion came from plowed-back earnings because the growth may be negligible. It is equally obvious that the companies such as Air Reduction, Borden, and Pillsbury Flour, whose reinvested incomes account for a small fraction of the expansion, financed their growth to an important extent from profits. In nearly one-half the cases, profits reinvested were equal to 50 per cent of total assets at January 1, 1922, and in many cases the assets increased more

TABLE 6—METHODS OF FINANCING EXPANSION
Seventy-Two Companies, 1922–30

| Name of Company | Source of Expansion Funds: Per Cent from Retained Earnings | Source of Expansion Funds: Per Cent from New Issues | Extent of Expansion from Retained Earnings* (Per Cent) |
|---|---|---|---|
| Allied Chemical & Dye Corp. | 100 | -0- | 42 |
| American Can Co. | 100 | -0- | 51 |
| Coca-Cola Co. | 100 | -0- | 117 |
| Deere & Co. | 100 | -0- | 37 |
| General Electric Co. | 100 | -0- | 44 |
| Hart, Schaffner & Marx | 100 | -0- | 44 |
| Hershey Chocolate Corp. | 100 | -0- | 121 |
| Hudson Motor Car Co. | 100 | -0- | 383 |
| Motor Wheel Corp. | 100 | -0- | 66 |
| Nash-Kelvinator Corp. | 100 | -0- | 268 |
| National Acme Co. | 100 | -0- | 5 |
| New York Air Brake Co. | 100 | -0- | 28 |
| Packard Motor Car Co. | 100 | -0- | 80 |
| Quaker Oats Co. | 100 | -0- | 63 |
| Reo Motor Car Co. | 100 | -0- | 78 |
| R. J. Reynolds Tobacco Co. | 100 | -0- | 107 |
| Sears, Roebuck & Co. | 100 | -0- | 85 |
| Spicer Manufacturing Corp. | 100 | -0- | 70 |
| Timken Roller Bearing Co. | 100 | -0- | 207 |
| United States Steel Corp. | 100 | -0- | 15 |
| F. W. Woolworth Co. | 100 | -0- | 108 |
| Worthington Pump & Machinery Corp. | 100 | -0- | 6 |
| Wm. Wrigley, Jr. Co. | 98 | 2 | 137 |
| Corn Products Refining Co. | 97 | 3 | 21 |

—Continued

[2] In many cases stocks or bonds were issued to provide funds for immediate expansion and the securities were then retired from retained income.

TABLE 6—Continued

| Name of Company | Source of Expansion Funds | | Extent of Expansion from Retained Earnings* (Per Cent) |
|---|---|---|---|
| | Per Cent from Retained Earnings | Per Cent from New Issues | |
| Pittsburgh Plate Glass Co. | 97 | 3 | 56 |
| Otis Elevator Co. | 95 | 5 | 98 |
| California Packing Corp. | 92 | 8 | 47 |
| American Brake Shoe & Foundry Co. | 89 | 11 | 45 |
| Electric Storage Battery Co. | 89 | 11 | 27 |
| Loose-Wiles Biscuit Co. | 86 | 14 | 39 |
| International Harvester Co. | 81 | 19 | 34 |
| General Motors Corp. | 80 | 20 | 119 |
| S. S. Kresge Co. | 78 | 22 | 228 |
| General Cigar Company, Inc. | 75 | 25 | 29 |
| May Department Stores Co. | 74 | 26 | 59 |
| United States Rubber Co. | 74 | 26 | 13 |
| Mathieson Alkali Works, Inc. | 71 | 29 | 75 |
| Westinghouse Electric & Manufacturing Co. | 71 | 29 | 40 |
| Mack Trucks, Inc. | 70 | 30 | 87 |
| Commercial Solvents Corp. | 69 | 31 | 38 |
| Lima Locomotive Works | 69 | 31 | 16 |
| American Tobacco Co. | 67 | 33 | 41 |
| Liggett & Myers Tobacco Co. | 66 | 34 | 58 |
| Chicago Pneumatic Tool Co. | 65 | 35 | 18 |
| J. I. Case Co. | 64 | 36 | 43 |
| J. C. Penney Co. | 64 | 36 | 371 |
| Owens-Illinois Glass Co. | 61 | 39 | 35 |
| Goodyear Tire and Rubber Co. | 58 | 42 | 32 |
| Fairbanks, Morse & Co. | 58 | 42 | 34 |
| National Biscuit Co. | 54 | 46 | 30 |
| Chrysler Corp. | 53 | 47 | 117 |
| Union Carbide & Carbon Corp. | 52 | 48 | 37 |
| Mullins Manufacturing Corp. | 50 | 50 | 57 |
| Allis-Chalmers Manufacturing Co. | 49 | 51 | 13 |
| Air Reduction Company, Inc. | 45 | 55 | 114 |
| Inland Steel Co. | 42 | 58 | 46 |
| Continental Can Company, Inc. | 41 | 59 | 108 |
| B. F. Goodrich Co. | 41 | 59 | 27 |
| Pillsbury Flour Mills Co. | 38 | 62 | 159 |
| E. I. du Pont de Nemours & Co. | 37 | 63 | 23 |
| Firestone Tire and Rubber Co. | 36 | 64 | 103 |
| Borden Co. | 35 | 65 | 104 |
| Crucible Steel Co. of America | 32 | 68 | 2 |
| Consolidated Cigar Company, Inc. | 29 | 71 | 91 |
| Wheeling Steel Corp. | 27 | 73 | 13 |
| Baldwin Locomotive Works | 27 | 73 | 9 |
| American Cyanamid & Chemical Corp. | 19 | 81 | 36 |
| Gulf States Steel Corp. | 18 | 82 | 16 |
| Bethlehem Steel Corp. | 18 | 82 | 17 |
| Republic Steel Corp. | 3 | 97 | 5 |
| American Locomotive Co. | -0- | 100 | -18† |
| American Car and Foundry Co. | -0- | -0- | -3† |

* 1922–30 retained earnings as a per cent of 1921 assets.
† Net liquidation.

than 100 per cent from profits retained in the nine profitable years.

Table 7 shows the percentage of total income retained by the various industries and the extent of expansion accounted for by earnings. Railway equipment companies as an industry distributed all earnings of the twenties. There was little expansion and new issues provided whatever funds were required. Steel manufacturers, industrial chemicals, and major tobacco companies each retained a small fraction of boom year profits. Retail merchandisers, can manufacturers, automobile manufacturers, and machinery manufacturers retained in industry aggregates unusually large portions of total income. Manufacturers of automobiles and machinery might expect highly fluctuating earnings due to cyclical factors and consequently retain earnings of profitable years to provide for rainy days, but the can manufacturing duopoly and retail merchandisers could hardly be included in the same category. It seems doubtful, therefore, that corporate management has considered seriously the nature of an industry and probable fluctuating income when formulating capital structures and consequent dividend policies. At least, other factors overshadow and render the stability of income of minor significance.

TABLE 7—SOURCES OF FUNDS FOR EXPANSION, BY INDUSTRIES

| Industry | Per Cent of Total Income Retained 1922–30 | Per Cent of Expansion Financed | |
|---|---|---|---|
| | | From Earnings | From New Issues |
| Railway equipment | 2 | 7 | 93 |
| Machinery manufacturing | 43 | 84 | 16 |
| Electrical equipment | 33 | 100 | -0- |
| Rubber manufacturing | 39 | 44 | 56 |
| Iron and steel | 28 | 51 | 49 |
| Iron and steel excluding United States Steel Corp. | 21 | 14 | 86 |
| Chrysler Corp. & General Motors Corp. | 36 | 75 | 25 |
| Other automobile manufacturing | 45 | 100 | -0- |
| Automobile equipment | 36 | 100 | -0- |
| Chemical producing | 28 | 55 | 45 |
| Metal container | 47 | 78 | 22 |
| Food processing | 35 | 67 | 33 |
| Retail merchandising | 55 | 94 | 6 |
| Major tobacco | 29 | 89 | 11 |
| Other tobacco and beverage | 36 | 100 | -0- |

It will be noted that new capital issues provided a small fraction of the financial requirements for growth in the rapidly expanding industries, and that industries with highest ratios of new capital compared to growth from profits in the prosperous twenties are those which were already overexpanded. Railway equipments, rubber, and iron and steel manufacturers had more new capital than retained income. The first two industries hardly enjoyed a decade which can be called prosperous, while steel companies perhaps require capital commitments in too large units to be financed easily from earnings.

*Net Income Retained, 1922–33*

Thus far we have examined corporate financing for growth during the profitable twenties and the record shows reinvested earnings as the principal source of capital and that practically all companies which were really profitable retained a substantial portion of income produced during the good years. If the period of time is extended three years, through 1933 for most companies, the percentage of total income retained throughout the complete cycle is much less, as demonstrated in Table 8.

TABLE 8—CLASSIFICATION OF COMPANIES BY PERCENTAGE OF EARNINGS RETAINED, 1922–33

| Per Cent Income Retained | Number of Companies |
|---|---|
| Losses | 9 |
| 0–20 | 22 |
| 21–30 | 18 |
| 31–40 | 15 |
| More than 41 | 8 |

There were only eight companies, or 11 per cent of the group, which retained more than 41 per cent of total income over the complete cycle, while 70 per cent of the companies retained less than one-third of total income. Twelve per cent of these enterprises actually lost part of their 1922 original capital during the twelve year period. However, over the complete cycle, twenty-seven of the seventy-two companies retained earnings which increased assets invested more than 50 per cent in spite of the severe depression.

Table 9 summarizes by industry the financial history of each company showing the total income, retained earnings, new stock and bond financing, and extent of reinvested earnings during the 1922–33 cycle. All factors discussed in this chapter are assembled for each company in the sample in the complete summary table on page 42.[8]

[8] The years of prosperity and depression are not the same for all companies. In order to facilitate discussion and comparison, Tables 4, 5, and 7 are based upon the period 1922–30. Where individual company experiences are emphasized the years of most profitable and least profitable operations for each company are used. This difference in prosperity and depression periods accounts for differences in figures in the various tables. In Table 9 and elsewhere the periods are: railway equipment, glass production, electrical equipment, auto equipment, chemical, metal containers, and foods, 1922–30, 1931–33; machinery manufacturing and iron and steel, 1922–30, 1931–34; Chrysler Corporation, 1922–29, 1930–32; General Motors, 1922–30, 1931–33; Packard, 1922–30, 1931–34; other automobile companies, 1922–29, 1930–34; tire and rubber, 1922–29, 1930–33; J. C. Penney, 1922–29, 1930–32; May Department Stores, 1922–30, 1931–32; other merchandisers, 1922–30, 1931–33; major tobaccos, 1922–32, 1933–36; miscellaneous tobacco and beverage companies, 1922–31, 1932–34.

TABLE 9—CORPORATE EXPANSION AND LIQUIDATION THROUGH PROSPERITY AND DEPRESSION
(Amounts in thousands of dollars)

| Industry | Total Earnings Prosperity Period | Growth of Corporate Assets, Profitable Period: Retained Earnings | | | | Growth of Corporate Assets, Profitable Period: New Capital | | | | Income after Dividends Depression Period | | Retained Earnings as a Per Cent of Total Earnings 1922–33 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Amount | Per Cent of Total Earnings | Per Cent of 1921 Assets | Per Cent of Growth Financed | Stocks | Bonds | Total | Per Cent of Growth Financed | Amount | Per Cent of Prosperity Period Retained Earnings | |
| **Railway equipment** | | | | | | | | | | | | |
| American Brake Shoe & Foundry Co. | $ 25,158 | $ 9,886 | 39 | 45 | 89 | $ 1,195 | $ 34 | $ 1,229 | 11 | $ −1,790 | 18 | 29 |
| American Car and Foundry Co. | 47,796 | −3,504 | –0– | −3 | –0– | –0– | | –0– | –0– | −10,131 | –0– | –0– |
| American Locomotive Co. | 48,700 | −15,133 | –0– | −18 | –0– | 41,167 | −1,912 | 39,255 | 100 | −15,666 | –0– | –0– |
| Baldwin Locomotive Works | 41,267 | 7,231 | 18 | 9 | 27 | 1,075 | 18,912 | 19,987 | 73 | −12,759 | 176 | –0– |
| Lima Locomotive Works, Inc. | 6,869 | 1,911 | 28 | 16 | 69 | 2,873 | −2,000 | 873 | 31 | −3,337 | 174 | –0– |
| New York Air Brake Co. | 13,078 | 3,981 | 30 | 28 | 100 | 307 | −3,001 | −2,694 | –0– | −1,221 | 31 | 23 |
| **Total** | $ 182,868 | $ 4,372 | 2 | 1 | 7 | $ 46,617 | $ 12,034 | $ 58,650 | 93 | $ −44,904 | –0– | –0– |
| **Machinery** | | | | | | | | | | | | |
| Allis-Chalmers Manufacturing Co. | $ 32,149 | $ 7,084 | 22 | 13 | 49 | $ −6,463 | $ 13,893 | $ 7,430 | 51 | $ −7,608 | 107 | –0– |
| J. I. Case Co. | 24,245 | 12,487 | 52 | 43 | 64 | 7,043 | –0– | 7,043 | 36 | −8,058 | 65 | 23 |
| Chicago Pneumatic Tool Co. | 9,458 | 3,144 | 33 | 18 | 65 | −933 | 2,601 | 1,668 | 35 | −931 | 30 | 24 |
| Deere & Co. | 54,088 | 28,848 | 53 | 37 | 100 | 23 | −10,057 | −10,034 | –0– | −13,593 | 47 | 34 |
| Fairbanks, Morse & Co. | 22,483 | 7,876 | 35 | 34 | 58 | −1,398 | 7,078 | 5,680 | 42 | −6,251 | 79 | 9 |
| International Harvester Co. | 186,211 | 81,832 | 44 | 34 | 81 | 20,780 | −1,892 | 18,888 | 19 | −49,485 | 60 | 18 |
| National Acme Co. | 3,105 | 1,630 | 53 | 5 | 100 | –0– | −3,131 | −3,131 | –0– | −2,261 | 139 | –0– |
| Otis Elevator Co. | 51,666 | 25,061 | 49 | 98 | 95 | 1,786 | −500 | 1,286 | 5 | −11,053 | 44 | 27 |
| Worthington Pump & Machinery Corp. | 10,892 | 1,938 | 18 | 6 | 100 | −1,400 | −1,486 | −2,886 | –0– | −5,860 | 302 | –0– |
| **Total** | $ 394,297 | $169,900 | 43 | 32 | 87 | $ 19,438 | $ 6,506 | $ 25,944 | 13 | $ −105,100 | 62 | 18 |
| **Glass products** | | | | | | | | | | | | |
| Owens-Illinois Glass Co. | $ 38,613 | $ 11,351 | 29 | 35 | 61 | $ 2,546 | $ 4,800 | $ 7,346 | 39 | $ 3,771 | –0– | 30 |
| Pittsburgh Plate Glass Co. | 99,978 | 34,316 | 34 | 56 | 97 | 959 | –0– | 959 | 3 | −197 | 1 | 32 |
| **Total** | $ 138,591 | $ 45,667 | 33 | 49 | 85 | $ 3,505 | $ 4,800 | $ 8,305 | 15 | $ 3,574 | –0– | 31 |
| **Electrical Equipment** | | | | | | | | | | | | |
| General Electric Co. | $ 423,593 | $130,432 | 31 | 44 | 100 | $ 8,094 | $ −35,958 | $ −27,864 | –0– | $ −38,926 | 30 | 18 |
| Westinghouse Electric Mfg. Co. | 160,486 | 62,458 | 39 | 40 | 71 | 61,725 | −36,249 | 25,476 | 29 | −38,576 | 61 | 17 |
| **Total** | $ 584,079 | $192,890 | 33 | 43 | 100 | $ 69,819 | $ −72,207 | $ −2,388 | –0– | $ −77,502 | 40 | 18 |
| **Tire and rubber** | | | | | | | | | | | | |
| Firestone Tire & Rubber Co. | $ 74,803 | $ 43,221 | 58 | 103 | 36 | $ 53,403 | $ 22,718 | $ 76,121 | 64 | $ −5,418 | 13 | 40 |
| B. F. Goodrich Co. | 76,729 | 22,775 | 30 | 27 | 41 | 26,915 | 6,277 | 33,192 | 59 | −25,231 | 111 | –0– |
| Goodyear Tire & Rubber Co. | 127,184 | 50,099 | 39 | 32 | 58 | 6,161 | 30,165 | 36,326 | 42 | −13,023 | 26 | 24 |
| United States Rubber Co. | 113,816 | 36,344 | 32 | 13 | 74 | 17,735 | −4,638 | 13,097 | 26 | −25,563 | 72 | 10 |
| **Total** | $ 392,532 | $152,439 | 39 | 27 | 49 | $ 104,214 | $ 54,522 | $ 158,736 | 51 | $ −69,235 | 45 | 19 |

**TABLE 9—Continued**

| Industry | Total Earnings Prosperity Period | Growth of Corporate Assets, Profitable Period: Retained Earnings: Amount | Retained Earnings: Per Cent of Total Earnings | Retained Earnings: Per Cent of 1921 Assets | Retained Earnings: Per Cent of Growth Financed | New Capital: Stocks | New Capital: Bonds | New Capital: Total | New Capital: Per Cent of Growth Financed | Income after Dividends Depression Period: Amount | Income after Dividends Depression Period: Per Cent of Prosperity Period Retained Earnings | Retained Earnings as a Per Cent of Total Earnings 1922–33 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Iron and steel** | | | | | | | | | | | | |
| Bethlehem Steel Co. | $ 263,526 | $ 58,289 | 22 | 17 | 18 | $ 281,324 | $ –20,437 | $ 260,887 | 82 | $ –44,048 | 76 | 4 |
| Crucible Steel Co. of America | 44,316 | 2,463 | 6 | 2 | 32 | –2,475 | 7,601 | 5,126 | 68 | –8,098 | 329 | –0– |
| Gulf States Steel Corp. | 8,524 | 2,466 | 29 | 16 | 18 | 5,634 | 5,386 | 11,020 | 82 | –1,513 | 61 | 14 |
| Inland Steel Co. | 64,148 | 22,198 | 35 | 46 | 42 | 7,025 | 23,039 | 30,064 | 58 | –2,360 | 11 | 27 |
| Republic Steel Corp. | 43,835 | 5,424 | 12 | 5 | 3 | 137,063 | 48,206 | 185,269 | 97 | –26,456 | 49 | –0– |
| United States Steel Corp. | 1,090,777 | 332,577 | 31 | 15 | 100 | 237,298 | –441,356 | –204,058 | –0– | –213,638 | 64 | 12 |
| Wheeling Steel Corp. | 50,197 | 10,989 | 22 | 13 | 27 | 4,635 | 24,480 | 29,115 | 73 | –9,669 | 88 | 3 |
| **Total** | $1,565,323 | $434,406 | 28 | 15 | 58 | $ 670,504 | $–353,081 | $ 317,423 | 42 | $ –305,782 | 70 | 9 |
| **Total excluding U. S. Steel Corp.** | 474,546 | 101,829 | 21 | 15 | 16 | 433,206 | 88,275 | 521,481 | 84 | –92,144 | 90 | 2 |
| **Automobile** | | | | | | | | | | | | |
| Chrysler Corp. | $ 112,469 | $ 65,935 | 59 | 117 | 52 | $ 21,938 | $ 38,421 | $ 60,359 | 48 | $ –29,418 | 45 | 35 |
| General Motors Corp. | 1,351,864 | 465,379 | 34 | 119 | 80 | 85,443 | 29,330 | 114,773 | 20 | –85,826 | 18 | 25 |
| Hudson Motor Car Co. | 89,688 | 46,971 | 52 | 383 | 100 | 139 | –0– | 139 | –0– | –22,860 | 49 | 32 |
| Mack Trucks, Inc. | 53,982 | 24,442 | 47 | 87 | 70 | 8,366 | 2,163 | 10,529 | 30 | –11,286 | 46 | 26 |
| Nash-Kelvinator Corp. | 127,281 | 56,575 | 44 | 268 | 100 | –20,380 | –0– | –20,380 | –0– | –20,439 | 36 | 26 |
| Packard Motor Car Co. | 119,872 | 40,536 | 34 | 74 | 100 | –14,834 | –9,854 | –24,688 | –0– | –20,374 | 50 | 24 |
| Reo Motor Car Co. | 31,830 | 13,001 | 41 | 78 | 100 | –344 | –0– | –344 | –0– | –12,163 | 94 | 4 |
| **Total** | $1,886,986 | $712,839 | 38 | 139 | 100 | $ 80,328 | $ 60,060 | $ 140,388 | –0– | $ –202,366 | 29 | 24 |
| **Auto equipment** | | | | | | | | | | | | |
| Electric Storage Battery Co. | $ 57,547 | $ 10,599 | 18 | 27 | 89 | $ 1,357 | –0– | $ 1,357 | 11 | $ –1,974 | 19 | 14 |
| Motor Wheel Corp. | 16,837 | 5,893 | 35 | 66 | 100 | –713 | –0– | –713 | –0– | –2,476 | 42 | 22 |
| Mullins Manufacturing Corp. | 2,982 | 1,937 | 65 | 57 | 50 | 1,907 | –0– | 1,907 | 50 | –400 | 21 | 56 |
| Spicer Manufacturing Corp. | 11,156 | 9,774 | 88 | 70 | 100 | –1,106 | $ –2,604 | –3,710 | –0– | –3,200 | 33 | 75 |
| Timken Roller Bearing Co. | 83,152 | 34,443 | 40 | 207 | 100 | –1,941 | –0– | –1,941 | –0– | –6,772 | 20 | 35 |
| **Total** | $ 171,674 | $ 62,646 | 36 | 76 | 100 | $ –496 | $ –2,604 | $ –3,100 | –0– | $ –14,822 | 24 | 27 |
| **Chemical** | | | | | | | | | | | | |
| Air Reduction Company, Inc. | $ 26,031 | $ 10,917 | 42 | 114 | 45 | $ 14,964 | $ –1,419 | $ 13,545 | 55 | $ –162 | 1 | 30 |
| Allied Chemical & Dye Corp. | 204,294 | 82,018 | 40 | 42 | 100 | 376 | –8,769 | –8,393 | –0– | –5,217 | 6 | 31 |
| American Cyanamid & Chemical Corp. | 16,191 | 5,858 | 36 | 36 | 19 | 17,730 | 6,693 | 24,423 | 81 | 3,339 | –0– | 47 |
| Commercial Solvents Corp. | 16,178 | 6,265 | 39 | 38 | 69 | 3,649 | –772 | 2,877 | 31 | 130 | –0– | 29 |
| E. I. du Pont de Nemours & Co. | 364,585 | 54,330 | 15 | 23 | 37 | 132,211 | –38,442 | 93,769 | 63 | –5,203 | 10 | 10 |
| Mathieson Alkali Works, Inc. | 14,436 | 7,904 | 55 | 75 | 71 | 3,193 | –33 | 3,160 | 29 | –454 | 6 | 42 |
| Union Carbide & Carbon Corp. | 215,838 | 70,075 | 33 | 37 | 52 | 63,617 | 1,632 | 65,249 | 48 | –3,927 | 6 | 26 |
| **Total** | $ 857,553 | $237,367 | 28 | 36 | 54 | $ 235,740 | $ –41,110 | $ 194,630 | 46 | $ –11,494 | 5 | 21 |

TABLE 9—Continued

| Industry | Total Earnings Prosperity Period | Growth of Corporate Assets, Profitable Period: Retained Earnings: Amount | Retained Earnings: Per Cent of Total Earnings | Retained Earnings: Per Cent of 1921 Assets | Retained Earnings: Per Cent of Growth Financed | New Capital: Stocks | New Capital: Bonds | New Capital: Total | New Capital: Per Cent of Growth Financed | Income after Dividends Depression Period: Amount | Income after Dividends Depression Period: Per Cent of Prosperity Period Retained Earnings | Retained Earnings as a Per Cent of Total Earnings 1922–33 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Metal container** | | | | | | | | | | | | |
| American Can Co. | $ 142,766 | $ 65,441 | 46 | 51 | 100 | $ –0– | $ –9,656 | $ –9,656 | –0– | $ 1,023 | –0– | 36 |
| Continental Can Company, Inc. | 49,093 | 24,491 | 50 | 108 | 41 | 35,452 | –0– | 35,452 | 59 | 6,115 | –0– | 45 |
| **Total** | $ 191,859 | $ 89,932 | 47 | 60 | 78 | $ 35,452 | $ –9,656 | $ 25,796 | 22 | $ 7,318 | –0– | 39 |
| **Food processing** | | | | | | | | | | | | |
| Borden Co. | $ 89,356 | $ 44,845 | 50 | 104 | 35 | $ 81,095 | $ 911 | $ 82,006 | 65 | $ –2,913 | 6 | 36 |
| California Packing Corp. | 46,647 | 16,433 | 35 | 47 | 92 | 1,385 | –0– | 1,385 | 8 | –14,757 | 90 | 4 |
| Corn Products Refining Co. | 107,844 | 27,708 | 26 | 21 | 97 | 1,289 | –519 | 770 | 3 | 335 | –0– | 20 |
| Hershey Chocolate Corp. | 54,321 | 37,172 | 68 | 121 | 100 | –16,464 | –9,349 | –25,813 | –0– | 2,482 | –0– | 56 |
| Loose-Wiles Biscuit Co. | 15,447 | 7,494 | 49 | 39 | 85 | 645 | 653 | 1,298 | 15 | 537 | –0– | 39 |
| National Biscuit Co. | 142,720 | 24,206 | 17 | 30 | 54 | 20,133 | 394 | 20,527 | 46 | –1,790 | 7 | 12 |
| Pillsbury Flour Mills Co. | 22,557 | 8,386 | 37 | 159 | 38 | 6,571 | 7,240 | 13,811 | 62 | 1,303 | –0– | 25 |
| Quaker Oats Co. | 58,903 | 21,370 | 36 | 63 | 100 | –0– | –0– | –0– | –0– | –978 | 5 | 27 |
| **Total** | $ 537,795 | $187,614 | 35 | 50 | 67 | $ 94,654 | $ –670 | $ 93,984 | 33 | $ –15,781 | 8 | 25 |
| **Merchandising** | | | | | | | | | | | | |
| Hart, Schaffner & Marx | $ 19,299 | $ 9,592 | 50 | 44 | 100 | $ –3,161 | $ –0– | $ –3,161 | –0– | $ –8,863 | 92 | 7 |
| S. S. Kresge Co. | 108,322 | 64,095 | 59 | 228 | 75 | 2,005 | 19,590 | 21,595 | 25 | –150 | –0– | 51 |
| May Department Stores Co. | 54,360 | 23,892 | 44 | 59 | 74 | 8,183 | –0– | 8,183 | 26 | –1,782 | 7 | 38 |
| J. C. Penney Co. | 60,825 | 36,617 | 60 | 371 | 64 | 20,328 | 137 | 20,465 | 36 | –5,516 | 15 | 37 |
| Sears, Roebuck & Co. | 170,483 | 106,938 | 63 | 85 | 100 | –393 | –33,297 | –33,690 | –0– | –8,626 | 7 | 65 |
| F. W. Woolworth Co. | 253,634 | 125,534 | 50 | 108 | 100 | –9,528 | 1,521 | –8,007 | –0– | –2,850 | 3 | 33 |
| **Total** | $ 666,923 | $366,668 | 55 | 106 | 99 | $ 17,434 | $ –12,049 | $ 5,385 | 1 | $ –27,787 | 8 | 44 |
| **Major tobacco** | | | | | | | | | | | | |
| American Tobacco Co. | $ 316,291 | $ 74,731 | 24 | 41 | 67 | $ 50,343 | $ –14,082 | $ 36,261 | 33 | $ –19,216 | 26 | 14 |
| Liggett & Myers Tobacco Co. | 213,256 | 65,164 | 31 | 58 | 66 | 34,408 | –1,393 | 33,015 | 34 | 2,883 | –0– | 25 |
| R. J. Reynolds Tobacco Co. | 314,562 | 88,862 | 28 | 96 | 100 | –38,329 | –0– | –38,329 | –0– | –29,164 | 33 | 15 |
| **Total** | $ 844,109 | $228,757 | 27 | 59 | 89 | $ 46,422 | $ –15,475 | $ 30,947 | 11 | $ –45,497 | 20 | 16 |
| **Miscellaneous** | | | | | | | | | | | | |
| Coca-Cola Co. | $ 92,559 | $ 37,335 | 40 | 117 | 100 | $ –25,392 | $ –82 | $ –25,474 | –0– | $ 8,907 | –0– | 36 |
| Consolidated Cigar Corp. | 28,868 | 6,820 | 24 | 91 | 29 | 16,205 | 338 | 16,543 | 71 | –249 | 4 | 20 |
| General Cigar Company, Inc. | 34,239 | 10,473 | 31 | 29 | 75 | 720 | 2,800 | 3,520 | 25 | –5,098 | 49 | 14 |
| Wm. Wrigley, Jr. Co. | 94,898 | 34,839 | 37 | 137 | 98 | –667 | 1,248 | 581 | 2 | 1,867 | –0– | 31 |
| **Total** | $ 250,564 | $ 89,467 | 36 | 88 | 100 | $ –9,134 | $ 4,304 | $ –4,830 | –0– | $ 5,427 | –0– | 30 |

## Chapter 3

# PROSPERITY EARNINGS AND DEPRESSION DIVIDENDS

Asset structure and economic activity of companies in the twelve industries differ greatly as already pointed out but in Chapter 2 it is demonstrated that the practice of retaining earnings is not peculiar to any industry. On the contrary, we see that reinvesting income is a policy of the individual companies and that in widely varying degree all the profitable companies in all the industries withheld income.

The purpose of this chapter is to determine whether ability to pay depression dividends was dependent upon the extent of 1922–30 profits retained, and to measure the amount of depression dividends paid from surplus accumulated during the twenties.

In determining the amount of depression dividends paid from reinvested prosperity earnings it is important to differentiate between reported income or loss and actual funds resulting from operations that affect dividend paying capacity, especially during the depression years. Write-downs of plant, security values, inventory, developmental costs, and intangible assets may represent long term business expenses, but the write-down as such in no way dissipates physical properties or liquid assets which could be used to meet current operating costs or dividend requirements even though such charges reduce the surplus balance. Appendix II explains the technique used to measure the profits retained during the twenties and the amount of depression dividends paid from these reinvested profits.[1]

### *Measurement of Dividend Performances*

Very few corporations pay a consistent and uniform dividend rate to common stockholders and it is therefore difficult to

[1] A thorough discussion of the nature and theory of surplus adjustments along with a number of historical records is presented by W. A. Hosmer of Harvard University in an article "The Effect of Direct Charges to Surplus on the Measurement of Income," *Business and Modern Society*, edited by Malcolm P. McNair (Harvard University Press, 1938).

describe the magnitude of a dividend reduction or increase from prosperity to depression. However, if dividends of $30,000 were paid in 1930 and $15,000 in 1931, there would be little hesitancy in saying the cut was 50 per cent. Over a much longer period of time capital structures may change in many diverse ways, such as through stock dividends, stock splits, new issues and retirements, and in addition the growth factor must be considered. For all practical purposes of portraying a relationship the rate of dividend cut can be computed for a period of years in the same manner as suggested for two specific years. Dividends paid by each company in 1927, 1928, 1929, and 1930 were added and divided by the number of years to provide the average annual dividend paid during the best years. Total dividends paid through depression years were divided by the number of years considered to be the worst of the poor years for each company, usually 1931–33, in order to arrive at average depression dividends.

*Twenty-Five Per Cent of Companies with Best 1931–33 Dividend Record*

A simple way to discover the amount of dividends paid from rainy day reserves is to divide the companies into groups based upon dividend maintenance during the poorest years. Table 10 presents in condensed summary the income and dividend records of nineteen companies that have the best depression dividend records since they actually increased the cash payments to common stockholders. It is very clear that corporations with the best depression dividend records operated profitably through the poorest years and in most cases found it unnecessary to draw upon the surplus.

There is nothing unusual about the portion of prosperity earnings retained by these companies that increased dividend payments during the poorest years. Each enterprise retained and reinvested part of the profits, but generous depression dividends were paid because these companies had no depression. There are three exceptions where dividends were paid materially in excess of reported income.[2]

[2] It is necessary at all times to recognize the distinction between accrued income or loss and funds made available from operations. Retained earnings are not held in liquid funds for the expressed purpose of meeting financial reverses,

TABLE 10—COMPARISON OF PROSPERITY EARNINGS RETAINED WITH DEPRESSION DIVIDENDS PAID
Nineteen Companies that Increased Common Dividend Payments during Depression Years
(Amounts in thousands of dollars)

| Company | Per Cent of Dividend Increase | Earnings Retained in Prosperity Period | | | Income and Dividends in Depression Period | | | | | | | Depression Dividends as a Per Cent of 1930 Assets |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | Excess of Dividends over Income | | | | |
| | | Amount | Per Cent of Total Net Income | Per Cent of Earnings Available to Common Stock | Reported Income after Interest | Adjusted Income after Interest | Preferred and Common Dividends | Reported | Adjusted | Excess as Per Cent of Earnings Retained in Prosperity Period | | |
| | | | | | | | | | | Reported | Adjusted | |
| Hershey Chocolate Corp. | 208.0 | $ 37,172 | 68 | 87 | $ 16,620 | $ 17,024 | $ 14,138 | -0- | -0- | -0- | -0- | 103.9 |
| General Cigar Company, Inc. | 77.0 | 10,473 | 31 | 41 | 5,114 | 6,297 | 10,212 | $ 5,098 | $ 3,915 | 48.7 | 37.4 | 31.4 |
| F. W. Woolworth Co. | 54.5 | 125,534 | 50 | 66 | 63,450 | 75,316 | 66,300 | 2,850 | -0- | 2.3 | -0- | 38.3 |
| Loose-Wiles Biscuit Co. | 37.1 | 7,494 | 49 | 66 | 5,352 | 5,779 | 4,815 | -0- | -0- | -0- | -0- | 17.3 |
| Coca-Cola Co. | 34.3 | 37,335 | 40 | 45 | 35,880 | 29,346 | 26,973 | -0- | -0- | -0- | -0- | 58.1 |
| Borden Co. | 31.8 | 44,845 | 50 | 59 | 28,259 | 37,400 | 31,172 | 2,913 | -0- | 6.5 | -0- | 19.0 |
| Air Reduction Company, Inc. | 20.5 | 10,918 | 42 | 42 | 9,302 | 12,790 | 9,465 | 163 | -0- | 1.5 | -0- | 28.0 |
| J. C. Penney Co. | 19.6 | 36,615 | 60 | 65 | 22,286 | 23,137 | 27,804 | 5,518 | 4,667 | 15.1 | 12.7 | 41.1 |
| Pillsbury Flour Mills Co. | 19.5 | 8,386 | 37 | 66 | 3,966 | 6,386 | 2,663 | -0- | -0- | -0- | -0- | 9.8 |
| Liggett & Myers Tobacco Co. | 16.6 | 65,164 | 31 | 37 | 77,881 | 78,286 | 75,001 | -0- | -0- | -0- | -0- | 44.0 |
| Continental Can Company, Inc. | 12.7 | 24,491 | 50 | 53 | 18,037 | 17,925 | 11,922 | -0- | -0- | -0- | -0- | 15.0 |
| American Can Co. | 12.5 | 65,442 | 46 | 57 | 41,844 | 41,405 | 40,821 | -0- | -0- | -0- | -0- | 22.1 |
| Mathieson Alkali Works, Inc. | 12.4 | 7,904 | 55 | 63 | 3,348 | 3,891 | 3,802 | 454 | -0- | 5.7 | -0- | 18.2 |
| S. S. Kresge Co. | 6.6 | 64,096 | 59 | 61 | 15,012 | 19,013 | 15,163 | 151 | -0- | 0.2 | -0- | 14.0 |
| Allied Chemical & Dye Corp. | 6.2 | 82,019 | 40 | 46 | 44,968 | 59,934 | 50,185 | 5,217 | -0- | 6.4 | -0- | 18.4 |
| R. J. Reynolds Tobacco Co. | 3.9 | 88,862 | 28 | 29 | 90,836 | 91,446 | 120,000 | 29,164 | 28,534 | 29.5 | 28.8 | 77.1 |
| Quaker Oats Co. | 3.7 | 21,370 | 36 | 44 | 15,582 | 18,159 | 16,560 | 978 | -0- | 4.6 | -0- | 28.4 |
| Wm. Wrigley, Jr. Co. | 1.5 | 34,839 | 37 | 37 | 22,479 | 22,054 | 20,612 | -0- | -0- | -0- | -0- | 35.9 |
| Commercial Solvents Corp. | 0.4 | 6,265 | 39 | 42 | 5,728 | 5,808 | 5,598 | -0- | -0- | -0- | -0- | 59.6 |
| Totals | | $779,224 | 42 | 46 | $525,944 | $571,396 | $553,206 | $52,506 | $37,116 | | | 32.4 |

General Cigar retained only 31 per cent of the prosperity period earnings but increased common dividend payments 77 per cent during the poorest years. The following summary reveals the extent of depression dividends paid from surplus:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–31 | $10,473,000 | $10,449,000 |
| Dividends in excess of earnings, 1932–34 | 5,098,000 | 3,915,000 |
| Balance retained | $ 5,375,000 | $ 6,534,000 |

The J. C. Penney Company paid a limited amount of dividends from surplus which deserves explanation. For eight years, 1922–29, the company reinvested 60 per cent of the total net income and in 1930 paid dividends equal to the amount paid in the three year period before or after this date. Earnings of 1930 were slightly more than one-half the dividends paid, but retained income in the year 1929 alone would supply the deficiency.

The R. J. Reynolds company retained 28 per cent of the 1922–32 profits and for the four years 1933–36 maintained dividend payments at the previously established rate. Earnings declined sharply and dividends paid include an appreciable portion of profits withheld in the better years as shown in the following summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–32 | $88,862,000 | $101,938,000 |
| Dividends in excess of earnings, 1933–36 | 29,164,000 | 28,534,000 |
| Balance available | $59,698,000 | $ 73,404,000 |

but are generally invested in expanding volume of business. When demand for the output falls off, prices are likely to be reduced in an effort to encourage more sales or production reduced in order to maintain prices. If sales prices are sufficiently low the peak volume of production can usually be maintained. With sales prices below the cost of production the revenue may be entirely adequate to maintain interest and dividends until the assets (inventories, supplies, and plant facilities) used in production are consumed. This type of reserve can be utilized to provide funds during poor years, but it is precisely what the business enterprise hopes to avoid. Adjusted figures showing the cash results of operation are included in the table to indicate the extent to which depression distributions were made from current operations even though reported earning figures may indicate a decidedly different result based upon accrual accounting.

There is little to indicate that these nineteen companies were able to pay generous depression dividends because they retained earnings during the twenties. They retained no more of the prosperity period income than many other companies that did not continue dividends, and the dividends of the early thirties were not paid extensively from surplus but came from current profits. General Cigar and R. J. Reynolds drew rather heavily against surplus for depression dividends but they retained a relatively small portion of prosperity profits and increased dividends in spite of their generous dividend policies of the twenties.

### *Thirty-Three Per Cent of Companies that Reduced Dividends Less than 65 Per Cent*

It would not be at all necessary to maintain dividends in full during the poorest years in order to justify the practice of retaining earnings in the good years and the stockholder might feel amply rewarded for his forbearance if during poor years he should receive 40 or 50 per cent of his regular dividend. In our sample there are twenty-four companies, one-third of the group, that reduced dividends during the poorest years less than 65 per cent based upon rates of the late twenties. These companies paid $983,635,000 in depression dividends and we are greatly interested to know what portion of the 1922–30 earnings these concerns retained and to what extent the depression dividends came from accumulated surplus. Table 11 presents these companies ranked in order of dividend maintenance and shows the amount of earnings retained during the twenties and the extent to which depression dividends depended upon these reinvested profits.

It should be noted that only six of the enterprises reported losses and that only in the cases of Westinghouse and California Packing was the reported loss of considerable magnitude. The data demonstrate that practically all of the corporations which maintained dividends through the depression were able to operate profitably during the poorest years. Nevertheless, several companies in this group paid dividends substantially in excess of current earnings and we shall examine these instances in greater detail.

**Table 11—Comparison of Prosperity Earnings Retained with Depression Dividends Paid**
**Twenty-Four Companies that Reduced Common Dividends Less than 65 Per Cent**
**(Amounts in thousands of dollars)**

| Company | Per Cent of Dividend Reduction | Earnings Retained in Prosperity Period: Amount | Earnings Retained in Prosperity Period: Per Cent of Total Net Income | Earnings Retained in Prosperity Period: Per Cent of Earnings Available to Common Stock | Income and Dividends in Depression Period: Reported Income after Interest | Income and Dividends in Depression Period: Adjusted Income after Interest | Income and Dividends in Depression Period: Preferred and Common Dividends | Excess of Dividends over Income: Reported | Excess of Dividends over Income: Adjusted | Excess as Per Cent of Earnings Retained in Prosperity Period: Reported | Excess as Per Cent of Earnings Retained in Prosperity Period: Adjusted | Depression Dividends as a Per Cent of 1930 Assets |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| National Biscuit Co. | 2.3 | $ 24,206 | 17 | 19 | $ 51,837 | $ 52,314 | $ 53,627 | $ 1,790 | $ 1,313 | 7.9 | 5.4 | 41.2 |
| Owens-Illinois Glass Co. | 7.0 | 11,351 | 29 | 33 | 11,659 | 24,001 | 7,888 | -0- | -0- | -0- | -0- | 17.6 |
| Corn Products Refining Co. | 7.5 | 27,708 | 26 | 30 | 30,977 | 28,104 | 30,642 | -0- | 2,538 | -0- | 9.2 | 25.3 |
| American Tobacco Co. | 12.7 | 74,731 | 24 | 27 | 87,078 | 87,968 | 106,294 | 19,216 | 18,330 | 25.7 | 24.5 | 36.6 |
| Goodyear Tire & Rubber Co. | 13.7 | 50,099 | 39 | 90 | 15,236 | 27,444 | 28,259 | 13,023 | 815 | 30.0 | 1.6 | 13.2 |
| Sears, Roebuck & Co. | 16.0 | 106,938 | 63 | 63 | 9,622 | 9,822 | 18,252 | 8,626 | 8,430 | 8.1 | 7.9 | 9.1 |
| General Electric Co. | 18.4 | 130,434 | 31 | 33 | 68,791 | 72,416 | 107,717 | 38,926 | 35,301 | 29.8 | 27.1 | 23.8 |
| Union Carbide & Carbon Corp. | 21.5 | 70,075 | 33 | 34 | 42,594 | 39,681 | 46,521 | 3,927 | 6,840 | 5.6 | 9.8 | 16.2 |
| E. I. du Pont de Nemours & Co. | 27.5 | 54,331 | 15 | 17 | 118,319 | 126,917 | 123,524 | 5,205 | -0- | 9.6 | -0- | 22.4 |
| Otis Elevator Co. | 32.5 | 25,062 | 49 | 52 | 655 | 2,943 | 11,709 | 11,054 | 8,766 | 44.1 | 35.0 | 22.6 |
| Chrysler Corp. | 34.2 | 65,935 | 59 | 62 | −9,551 | 6,420 | 19,869 | 29,420 | 13,449 | 44.6 | 20.4 | 10.4 |
| International Harvester Co. | 37.7 | 81,832 | 44 | 57 | −4,174 | −4,307 | 45,312 | 49,486 | 49,619 | 60.5 | 60.6 | 12.9 |
| American Brake Shoe & Foundry Co. | 38.8 | 9,886 | 39 | 52 | 2,629 | 3,485 | 4,419 | 1,790 | 934 | 18.1 | 9.4 | 13.4 |
| May Department Stores Co. | 39.1 | 23,891 | 44 | 46 | 3,145 | 3,732 | 4,927 | 1,782 | 1,195 | 7.5 | 5.0 | 6.9 |
| Firestone Tire & Rubber Co. | 43.7 | 43,221 | 58 | 74 | 15,119 | 13,112 | 20,537 | 5,418 | 7,425 | 12.5 | 17.2 | 13.4 |
| Westinghouse Electric Manufacturing Co. | 44.4 | 62,458 | 39 | 44 | −21,196 | −16,728 | 17,380 | 38,576 | 34,108 | 61.8 | 54.6 | 7.5 |
| Timken Roller Bearing Co. | 45.0 | 34,443 | 40 | 40 | 4,261 | 8,776 | 11,033 | 6,772 | 2,257 | 19.7 | 6.6 | 22.7 |
| General Motors Corp. | 45.9 | 465,378 | 34 | 36 | 180,256 | 269,990 | 266,080 | 85,824 | -0- | 18.4 | -0- | 26.6 |
| Pittsburgh Plate Glass Co. | 50.4 | 34,316 | 34 | 36 | 7,235 | 8,481 | 7,433 | 198 | -0- | 0.6 | -0- | 7.8 |
| California Packing Corp. | 58.1 | 16,433 | 35 | 35 | −9,870 | −7,778 | 4,887 | 14,757 | 12,665 | 89.8 | 77.1 | 9.3 |
| Nash-Kelvinator Corp. | 58.6 | 56,575 | 44 | 46 | 10,625 | 16,454 | 31,064 | 20,439 | 14,610 | 36.1 | 25.8 | 56.3 |
| Lima Locomotive Works, Inc. | 59.5 | 1,911 | 28 | 28 | −2,952 | −3,086 | 385 | 3,337 | 3,471 | 174.6 | 181.6 | 2.6 |
| Electric Storage Battery Co. | 61.4 | 10,599 | 18 | 18 | 6,082 | 7,760 | 8,026 | 1,974 | 356 | 18.6 | 3.4 | 21.0 |
| Mack Trucks, Inc. | 64.0 | 24,441 | 47 | 47 | −3,435 | −1,313 | 7,850 | 11,285 | 9,163 | 46.2 | 37.5 | 12.8 |
| Totals | | $1,506,254 | 34 | 38 | $614,492 | $776,608 | $983,635 | $372,825 | $231,585 | | | 20.7 |

American Tobacco has for many years been a generous dividend payer, disbursing 73 per cent of the available income from 1922 through 1932. Each year since 1932 earnings have been inadequate to meet the established dividend requirements and stockholders have received a portion of the retained income as shown in the following summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Earnings retained, 1922–32 | $74,731,000 | $73,906,000 |
| Dividends in excess of earnings, 1933–36 | 19,216,000 | 18,330,000 |
| Balance retained | $55,515,000 | $55,576,000 |

Sears Roebuck is sometimes used to illustrate the practice of paying dividends in poor years from surplus accumulated during good years, and it is true that this company did pay almost ten millions in cash dividends in excess of the depression income. Dividends paid in 1931 were earned in full, but in 1932 one-half the regular rate was paid in the face of operating losses. The summary emphasizes that a very small part of the prosperity retained earnings was used to pay depression dividends. If the stockholder must forego almost two-thirds of his income during seven fat years in order to receive one-half that rate in one lean year, possibly the price of the depression dividend is too great.

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $106,939,000 | $107,008,000 |
| Dividends in excess of earnings, 1931–32 | 8,626,000 | 8,430,000 |
| Balance retained | $ 98,313,000 | $ 98,578,000 |

Manufacture of electrical equipment is concentrated largely in the plants of two huge corporations and the product consists of heavy machinery and durable consumer goods. In nine prosperous years of the twenties General Electric paid $265,362,000 to common stockholders (counting $20,669,000 book value of Electric Bond & Share stock as cash equivalent) and reported $130,434,000 as retained. If reported figures are accepted as

final, only one-third of the earnings were retained but reserves for general contingencies increased nearly $30,000,000 and profit on sale of securities was $15,000,000. In addition to earnings retained, depreciation charges of $20,669,000 were not expended for plant maintenance and this additional amount became available for other corporate uses. After all adjustments the stockholders received 56 cents of each dollar made available through operations and the company reinvested 44 cents.

General Electric did not report an operating loss at any time but profits after 1930 were substantially reduced. Dividends during four years of the depression were maintained at 82 per cent of the prosperity level counting as cash $26,440,000 of Radio Corporation of America common stock distributed under consent decree. Common stockholders received $38,926,000 in cash dividends which were not earned during the depression. When one recalls that $208,019,000 was withheld in the twenties the dividends in excess of earnings do not appear overly impressive. The box score is as follows:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $130,434,000 | $208,019,000 |
| Dividends in excess of earnings, 1931–33 | 38,926,000* | 35,301,000* |
| Balance retained | $ 91,508,000 | $172,718,000 |

*Includes $7,725,000 preferred dividends and $1,157,000 interest.

Westinghouse Electric and Manufacturing Company retained 44 per cent of earnings available to stockholders during the prosperous decade (39 per cent of total net income) and suffered severe operating losses from 1931 to 1934. In spite of these losses, dividends were maintained equal to 56 per cent of boom period distribution. Retained funds of $58,104,000 were drawn upon for $17,380,000 to pay dividends during the early thirties and stockholders thereby received 30 per cent of the cash income previously withheld. Among the manufacturers of durable and capital goods Westinghouse is unique in its 1931–33 record. In spite of severe losses, substantial dividends were

paid, and as a result 62 per cent of the surplus created in nine good years was absorbed by losses and dividends during three poor years. This company paid relatively generous dividends during the twenties and still was able to make unusual dividend payments in the poorest years. The summary is as follows:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $62,458,000 | $58,104,000 |
| Losses, 1931–33 | 21,197,000 | 16,728,000 |
| Preferred dividends, 1931–33 | 737,000 | 737,000 |
| Common dividends, 1931–33 | 16,643,000 | 16,643,000 |
| Balance retained | $23,881,000 | $23,996,000 |

Two of the equipment manufacturers paid depression dividends approaching the regular rates established during the twenties. International Harvester and Otis Elevator each reported very small depression losses but each had retained a substantial portion of the prosperity profits. International Harvester is one of the largest companies in this sample and the record deserves emphasis because International Harvester is one of the noted corporations that paid dividends throughout the depression. Forty-four per cent of reported net income was retained during the good years. Common stockholders saw 57 per cent of reported earnings available for dividends reinvested and when adjustments are made for increases in surplus reserves the stockholder received one-third of the income actually available for dividends. Substantial operating loss was sustained in 1932 but stockholders received dividends at 58 per cent of the former rate. In total, common stockholders received 18 per cent of the income withheld in nine profitable years and only two-thirds of the amount retained in 1929 and 1930. When boiled down to bare facts the common stockholder may read the following box score:

| | *Reported* | *Adjusted* |
|---|---|---|
| Total net income reported, 1922–30 | $186,211,000 | $186,211,000 |
| Surplus reserve increase | | 12,276,000 |
| Secret reserve increase | | 31,000,000 |
| Total available, 1922–30 | | $229,487,000 |

| | | |
|---|---|---|
| Preferred Dividends, 1922–30 | 42,564,000 | 42,564,000 |
| Available to common | $143,647,000 | $186,923,000 |
| Common dividends | 61,815,000 | 61,815,000 |
| Retained earnings | $ 81,832,000 | $125,108,000 |
| Losses, 1931–34 | 4,174,000 | 4,307,000 |
| Balance available | $ 77,658,000 | $120,801,000 |
| Preferred dividends, 1931–34 | 22,900,000 | 22,900,000 |
| Common dividends, 1931–34 | 22,412,000 | 22,412,000 |
| Balance retained | $ 32,346,000 | $ 75,489,000 |

International Harvester operated at a loss only in 1932 and unexpended depreciation represents at least one-third of the reported loss. Even if we combine all preferred and common depression dividends in excess of funds produced, stockholders received only 36 cents of each dollar withheld during the twenties.

Otis Elevator paid dividends each of the depression years and stockholders received during the poorest years 68 per cent of their regular dividends. In better times the company retained fully one-half the total earnings. During the "years of the locust" minor operating losses were reported but depreciation charges continued while plant expenditures were negligible, indicating that funds from operations were an important factor in making dividend payments. Earnings withheld over a period of nine years aggregate $25,062,000 and $11,054,000 of the amount was later disbursed which is 44 per cent of the reported earnings withheld.

The summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $25,062,000 | $24,945,000 |
| Preferred dividends in excess of earnings, 1931–34 | 905,000 | –0– |
| Common dividends in excess of earnings, 1931–34 | 10,149,000 | 8,766,000 |
| Balance retained | $14,008,000 | $16,179,000 |

American Brake Shoe and Foundry is the only railway equipment company included which even approached consistency in maintaining dividends through the depression and this accomplishment can be accounted for through two contributing factors. Unlike other companies in the industry, no operating losses occurred during the depression years, and in addition, 51½ per cent of prosperity earnings available for dividends (39 per cent of total income) was withheld. It is very impressive to say the company paid four times as much in dividends as was earned during the three depression years and there is no intent here to minimize the accomplishment, but in round numbers and summary form the record shows:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $9,886,000 | $9,828,000 |
| Dividends in excess of earnings, 1931–34 | 1,790,000 | 934,000 |
| Balance retained | $8,096,000 | $8,894,000 |

In this group of companies that maintained dividends we find a number of motor car manufacturers. The Chrysler Corporation as such did not exist until 1925 and in order to make the data comparable the Maxwell figures are used before 1925 because in the beginning Chrysler was nothing more than the reorganized Maxwell Motor Car Company. Chrysler earnings in 1930 were at a low point while dividends greatly exceeded earnings and this condition continued until 1933. In the very profitable years before 1930 Chrysler retained 62 per cent of earnings available to common stockholders and 59 per cent of total net income. When the bad years came, dividends were maintained at 65 per cent of the boom year levels. During three of the poorest years in automobile history Chrysler stockholders received 30 per cent of the profits withheld during the twenties. The Chrysler record of remarkable dividend payments through the depression adds emphasis to the prerequisites already suggested for such disbursements. Fifty-nine per cent of the 1922–29 total net income was retained. No loss of funds occurred through operations during the worst years (since

unexpended depreciation is more than reported losses), and not more than 30 per cent of formerly retained earnings was disbursed. It may be significant to observe that 1936 Chrysler dividends were equal in amount to two-thirds of all dividends paid over the fourteen year period 1922–35 and is identical with the total dividends paid in the five year boom period 1926–30.

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–29 | $65,935,000 | $73,939,000 |
| Common dividends in excess of earnings, 1930–32 | 19,869,000 | 13,449,000 |
| Balance available | $46,066,000 | $60,490,000 |
| Losses, 1930–32 | 9,551,000 | –0– |
| Balance retained | $36,515,000 | $60,490,000 |

General Motors Corporation, second largest of the seventy-two companies included in this sample, earned more than $1,250,000,000 available for common dividends in the nine years 1922–30 and stockholders received regularly an average of 65 per cent of the annual earnings. Through the three worst years of the depression dividends were reduced 46 per cent. From each of the 469,034,000 prosperity dollars retained, stockholders received during the "rainy days" 18.3 cents. Approximately one-third of the dividends paid were in excess of reported income. All funds necessary for those disbursements came from operations since unexpended depreciation added to reported income exceeds cash dividends distributed. Once again it is demonstrated that a small part of profits withheld in good years reached stockholders during the thirties and that dividends paid during the depression were made available through the operating process and did not come from a storehouse of reserves or liquid assets. The summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $465,378,000 | $469,034,000 |
| Dividends in excess of earnings, 1931–33 | 85,824,000 | –0– |
| Balance retained | $379,554,000 | $469,034,000 |

Nash Motor Car Company[8] is somewhat famous for its highly liquid asset structure. For years during the twenties the cash balance alone was greater than all plant assets and when combined with marketable securities the liquid assets were twice as great as all other assets. From 1922–29 Nash retained 44 per cent of all earnings. In 1930 about one-half the dividend requirement was earned and dividends were reduced some 20 per cent. Through the bad years of 1931–34 dividends were maintained on an average at 41 per cent of 1926–29 rates. In spite of drastic reductions the payments far exceeded reported earnings and absorbed $14,610,000 of the $59,000,000 of funds retained during the twenties. The summary shows no exception to the assertion that a large part of income during the twenties did not reach the stockholder during the depression years, regardless of how invested.

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–29 | $56,575,000 | $58,813,000 |
| Dividends in excess of earnings, 1930–34 | 20,439,000 | 14,610,000 |
| Balance retained | $36,136,000 | $44,203,000 |

Mack Trucks, like the other automobile producers just reviewed, operated profitably through the twenties, retained a large fraction of the earnings, and continued to pay at least some dividends each year of the early thirties. Mack reported operating losses during the poorest years and undoubtedly drew upon the surplus to pay whatever dividends were distributed, but again it is obvious that the stockholder paid dearly for his small depression dividend in terms of income withheld during the twenties.

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–29 | $24,441,000 | $23,941,000 |
| Losses, 1930–34 | 3,435,000 | 1,313,000 |
| Balance available | $21,006,000 | $22,628,000 |
| Dividends, 1930–34 | 7,850,000 | 7,850,000 |
| Balance retained | $13,156,000 | $14,788,000 |

[8] Now Nash-Kelvinator.

In the rubber industry 1930 was a very unprofitable year and thereafter through 1933 conditions were poor. During this time, as can be seen from Table 11, Firestone reported moderate income but paid substantial dividends in excess of the earnings. The Firestone dividend record is far superior to that of other companies in the industry, but it demonstrates again that extensive dividends are not paid in excess of current income. Through four years of greatly curtailed operations Firestone disbursed to common stockholders $7,425,000 in excess of earnings which is 20 per cent of the $37,466,000 retained in the eight preceding years. The summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–29 | $43,221,000 | $37,466,000 |
| Common dividends in excess of earnings, 1930–33 | 5,418,000 | 7,425,000 |
| Balance retained | $37,803,000 | $30,041,000 |

As a final illustration of companies that paid moderate dividends through the depression let us examine the record of California Packing Company. This company retained a small fraction of the 1922–30 earnings and has a good depression record of dividends paid in spite of generous payments during the twenties. Dividends in 1931 were paid at the usual rate but in 1932 and 1933 when operations were conducted with heavy losses dividends were greatly curtailed and finally omitted in 1933. California Packing Company retained a very moderate 35 per cent of 1922–30 earnings, paid dividends far in excess of earnings through the depression but ceased payments when severe losses were incurred, financed heavily with funded debt in 1931, and resumed dividends in 1934 at the first sign of profits. The summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $16,433,000 | $16,433,000 |
| Operating losses, 1931–33* | 9,870,000 | 7,778,000 |
| Dividends in excess of earnings, 1931–33 | 4,887,000 | 4,887,000 |
| Balance retained | $ 1,676,000 | $ 3,768,000 |

*Contains $2,500,000 bond interest.

The prosperity and depression earnings and dividends of the twenty-four companies presented in Table 11 is a remarkable display of operating results. Each of these companies paid dividends in the early thirties that resulted in surplus charges with the exception of Owens-Illinois Glass and Corn Products. The important point, however, is that only a fraction of the previously withheld earnings was used to pay dividends. During the depression stockholders received 24.5 per cent of the billion and a half dollars earned and reinvested during the twenties. In the poorest years of the most severe depression in history these companies charged $372,825,000 of their dividend payments against surplus, and if we look no further this is a most impressive achievement. When we add the comment that these same companies paid $610,810,000 additional dividends that they earned during the poorest years according to their reported figures and that funds received through operations were greatly in excess of the reported earnings, dividends charged to surplus do not seem so impressive, especially when we remember that dividend payments were reduced substantially and that the $372,825,000 is less than 25 per cent of the earnings withheld during the twenties.

Of even more significance, there seems to be no relation between the ability to pay depression dividends and the amount of earnings previously retained. These companies maintained moderate dividend payments during the early thirties because in most cases they were able to operate with moderate success.

### *Forty Per Cent of Companies with Poorest Depression Dividend Records*

Twenty-nine of the seventy-two corporations in this sample made drastic reductions in dividend payments during the early thirties and we find one important and outstanding factor which explains the inability to continue dividends. The earnings withheld and reinvested during the twenties were lost during the poor years and hence could not possibly be used for dividends. In Table 12 the companies are arranged in order of dividend maintenance and the prosperity earnings retained are related to depression dividends paid.

TABLE 12—COMPARISON OF PROSPERITY EARNINGS RETAINED WITH DEPRESSION DIVIDENDS PAID
Twenty-Nine Companies that Reduced Common Dividends More than 70 Per Cent
(Amounts in thousands of dollars)

| Company | Per Cent of Dividend Reduction | Earnings Retained in Prosperity Period | | | Income and Dividends in Depression Period | | | | | | | Depression Dividends as a Per Cent of 1930 Assets |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | | Excess of Dividends over Income | | | | |
| | | Amount | Per Cent of Total Net Income | Per Cent of Earnings Available to Common Stock | Reported Income after Interest | Adjusted Income after Interest | Preferred and Common Dividends | Reported | Adjusted | Excess as Per Cent of Earnings Retained in Prosperity Period | | |
| | | | | | | | | | | Reported | Adjusted | |
| American Car and Foundry Co. | 76.4 | $ −3,504 | −0− | −0− | $ −3,381 | $ −2,450 | $ 6,750 | $ 10,131 | $ 9,200 | −0− | −0− | 6.3 |
| Hudson Motor Car Co. | 78.2 | 46,970 | 52 | 52 | −14,744 | −9,802 | 8,115 | 22,859 | 17,917 | 48.7 | 38.1 | 13.6 |
| Deere & Co. | 79.0 | 28,848 | 53 | 87 | −8,716 | −4,806 | 4,877 | 13,593 | 9,683 | 47.1 | 33.6 | 5.7 |
| Inland Steel Co. | 79.2 | 22,198 | 35 | 40 | 1,840 | 1,840 | 4,200 | 2,360 | 2,360 | 10.6 | 10.6 | 4.2 |
| Allis-Chalmers Manufacturing Co. | 79.4 | 7,084 | 22 | 31 | −5,632 | −5,816 | 1,976 | 7,608 | 7,792 | 107.4 | 110.0 | 2.9 |
| B. F. Goodrich Co. | 79.7 | 22,775 | 30 | 74 | −19,546 | −19,928 | 5,685 | 25,231 | 25,613 | 110.8 | 112.5 | 4.3 |
| Reo Motor Car Co. | 79.8 | 13,001 | 41 | 41 | −9,791 | −8,708 | 2,372 | 12,163 | 11,080 | 93.6 | 85.2 | 8.9 |
| Bethlehem Steel Co. | 82.5 | 58,289 | 22 | 53 | −27,474 | −19,490 | 16,574 | 44,048 | 36,064 | 75.6 | 61.9 | 2.5 |
| United States Steel Corp. | 83.5 | 332,577 | 31 | 46 | −116,307 | −31,459 | 97,331 | 213,638 | 128,790 | 64.2 | 38.7 | 4.3 |
| J. I. Case Co. | 83.6 | 12,487 | 52 | 78 | −5,241 | −7,563 | 2,817 | 8,058 | 10,380 | 64.5 | 83.1 | 5.6 |
| Motor Wheel Corp. | 83.7 | 5,893 | 35 | 37 | −1,637 | −1,273 | 839 | 2,476 | 2,112 | 42.0 | 35.8 | 6.2 |
| Packard Motor Car Co. | 84.0 | 40,536 | 34 | 36 | −13,628 | −7,669 | 6,746 | 20,374 | 14,415 | 50.3 | 35.6 | 10.3 |
| Hart, Schaffner & Marx | 87.5 | 9,592 | 50 | 51 | −8,263 | −8,534 | 600 | 8,863 | 9,134 | 92.4 | 95.2 | 2.1 |
| Fairbanks, Morse & Co. | 93.1 | 7,876 | 35 | 46 | −5,525 | −5,411 | 726 | 6,251 | 6,137 | 79.4 | 77.9 | 2.0 |
| National Acme Co. | 93.2 | 1,629 | 53 | 53 | −2,161 | −1,545 | 100 | 2,261 | 1,645 | 138.8 | 101.0 | 1.0 |
| New York Air Brake Co. | 93.7 | 3,981 | 30 | 39 | −1,052 | −863 | 169 | 1,221 | 1,032 | 30.7 | 25.9 | 1.2 |
| American Locomotive Co. | 95.3 | −15,133 | −0− | −0− | −10,410 | −10,474 | 5,256 | 15,666 | 15,730 | −0− | −0− | 5.3 |
| Consolidated Cigar Corp. | 96.3 | 6,820 | 24 | 44 | 2,212 | 857 | 2,461 | 249 | 1,604 | 3.6 | 23.5 | 8.6 |
| American Cyanamid & Chemical Corp. | 100.0 | 5,858 | 36 | 46 | 3,339 | 3,529 | −0− | −0− | −0− | −0− | −0− | −0− |
| Baldwin Locomotive Works | 100.0 | 7,231 | 28 | 36 | −12,059 | −9,649 | 700 | 12,759 | 10,349 | 176.4 | 143.1 | 0.7 |
| Chicago Pneumatic Tool Co. | 100.0 | 3,144 | 33 | 46 | −931 | −141 | −0− | 931 | 141 | 29.6 | 4.5 | −0− |
| Crucible Steel Co. of America | 100.0 | 2,463 | 6 | 10 | −5,910 | −3,276 | 2,188 | 8,098 | 5,464 | 328.8 | 221.8 | 1.9 |
| Gulf States Steel Corp. | 100.0 | 2,466 | 29 | 39 | −1,478 | 937 | 35 | 1,513 | −0− | 61.4 | −0− | 0.1 |
| Republic Steel Corp. | 100.0 | 5,424 | 12 | 35 | −26,026 | −262 | 430 | 26,456 | 692 | 487.8 | 12.8 | 0.2 |
| Wheeling Steel Corp. | 100.0 | 10,989 | 22 | 83 | −7,771 | −1,367 | 1,898 | 9,669 | 3,265 | 88.0 | 29.7 | 1.6 |
| United States Rubber Co. | 100.0 | 36,344 | 32 | 100 | −25,541 | −25,972 | 22 | 25,563 | 25,994 | 70.3 | 71.5 | 0.1 |
| Mullins Manufacturing Corp. | 100.0 | 1,937 | 65 | 100 | −249 | −1,012 | 151 | 400 | 1,163 | 20.7 | 60.0 | 2.3 |
| Spicer Manufacturing Corp. | 100.0 | 9,774 | 88 | 100 | −2,440 | −9 | 760 | 3,200 | 769 | 32.7 | 7.9 | 5.8 |
| Worthington Pump & Machinery Corp. | 100.0 | 1,938 | 18 | 100 | −4,596 | −4,304 | 1,264 | 5,860 | 5,564 | 302.4 | 287.1 | 4.7 |
| Totals | | $689,487 | 29 | 46 | $−333,118 | $−184,620 | $175,042 | $511,499 | $364,089 | | | 3.6 |

In most cases these enterprises were highly profitable during the twenties and as a group and individually they retained a substantial portion of the 1922–30 profits. In contrast with the continuously profitable companies that maintained depression dividends, this group suffered severe losses and of course could not and should not have maintained dividend payments during the poor years. Some of the depression losers did pay substantial depression dividends, however, and we shall examine in detail the records of a number of the outstanding cases.

There are four railway equipment manufacturers listed in Table 12 and each paid at least some dividends during the early thirties, but it is disconcerting to try to establish causal relationship between these dividends and earnings withheld during the twenties. American Car & Foundry and American Locomotive operated with intermittent profits during the best years of the twenties and during that time did not earn the dividends in full. The depression dividends clearly did not come from earnings of the twenties but were in reality liquidating dividends.[4] This evidence supports the contention made earlier to the effect that dividends can be paid from capital as well as from surplus provided the funds are available. Unlike the two companies just discussed, Baldwin Locomotive and New York Air Brake each reinvested several millions of the profits of the twenties. In 1931 when losses were first experienced, Baldwin paid one-half the preferred dividends but thereafter no dividends were paid through the period under review because there were no earnings available for dividends. The record of New York Air Brake is very similar to that of Baldwin Locomotive. With no bonds or preferred stock in the capital structure, Air Brake paid a small dividend to common stockholders in 1931, but no further disbursements were made until 1936 when operating profits were again reported.[5] Surely there is nothing in the records of these four railway equipment manufacturers to indicate that

[4] American Locomotive reduced the par value of common stock from $50 to $5 per share.

[5] There is no intent to imply that these companies should have paid depression dividends at the 1927–30 rates. The purpose of common stock financing is to provide flexibility in paying for capital invested and it is therefore illogical and inconsistent to reason that income withheld in the good years will be used to pay dividends during the poor years.

retention of prosperity profits is essential to depression dividends or that such retention assures depression dividends.

Steel manufacturers operated profitably through the twenties and generally retained a large fraction of the earnings, but we find these enterprises prominently represented in the group of corporations that reduced dividends most during the poor years. Inland Steel is the only one of the smaller producers that paid any common dividends during the early thirties. Unlike the other companies, Inland reported a profit for the 1931–34 period which made the payments possible. Inland retained 35 per cent of net income for nine profitable years retaining in total $22,198,000. Dividends to common stock were reduced 79 per cent through 1931–34 and in aggregate required $2,360,000 of the funds formerly withheld or little more than 10 per cent.

Bethlehem, Crucible, and Republic are representative of the larger and more profitable steel corporations, but Bethlehem is the only one which paid substantial depression dividends. Bethlehem retained 53 per cent of good year earnings available to common and paid dividends for only one year when operating losses appeared. Of the $53,525,000 in funds retained, common stockholders eventually received $6,400,000 or 12 per cent. Through the twenties senior securities absorbed some 60 per cent of net income and the corporation reinvested only 22 per cent of the total income. With heavy bonded debt and severe operating loss in 1932 it is not surprising to find both preferred and common dividends omitted. The summary demonstrates that a limited amount of income retained in the profitable period reached stockholders during the early thirties.

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $58,289,000 | $53,525,000 |
| Income reported, 1931–34 | 354,000 | –0– |
| Interest charges, 1931–34 | 27,829,000 | 21,214,000 |
| Balance available | $30,814,000 | $32,311,000 |
| Preferred dividends, 1931–34 | 10,174,000 | 8,450,000 |
| Common dividends, 1931–34 | 6,400,000 | 6,400,000 |
| Balance retained | $14,241,000 | $17,461,000 |

Bethlehem paid less in common and preferred dividends combined when the poor years came than was retained in 1929 alone, and it will be noticed that dividend payments were suspended during the first year of poor business. This does not prove that more dividends should have been paid during the twenties, but it does support the contention that surplus from the good years is not used extensively to pay dividends during poor years.[6]

United States Steel retained 46 per cent of 1922–30 earnings available to common stockholders (31 per cent of total income), yet common dividends were omitted during the first year of poor operations and preferred dividends reduced to about 28 per cent of the agreed rate. In 1931 common stockholders received 11 per cent of the $332,577,000 reported income withheld or 16 per cent of the 1922–30 adjusted retained earnings, and none thereafter. On the other hand, $95,308,000 of the reinvested profits were lost. The summary:

| | *Reported* | *Adjusted* |
|---|---|---|
| Retained earnings, 1922–30 | $332,577,000 | $312,574,000 |
| Losses, 1931–34 | 95,308,000 | 10,460,000 |
| Bond interest, 1931–34 | 20,998,000 | 20,998,000 |
| Balance available | $216,271,000 | $281,116,000 |
| Preferred dividends, 1931–34 | 60,348,000 | 60,348,000 |
| Common dividends, 1931–34 | 36,984,000 | 36,984,000 |
| Balance retained | $118,939,000 | $183,784,000 |

Although depression dividend payments were drastically reduced on the preferred stock and omitted entirely on the common, United States Steel paid nearly $100,000,000 in cash

[6] The proposition can be made that common stockholders are in a better position since it is possible to pay bond interest and thereby keep control in the common. This procedure keeps control in the hands of corporate directors and officers, but the many small investors who own much of the common stock would have perhaps equally as much control if a trustee in bankruptcy were operating the enterprise. Furthermore, if the retained earnings are invested largely in inventories and plant facilities thereby setting the stage for a slump, it might be healthy to drain the profits off in the form of cash dividends and avoid or mitigate a period of forced liquidation. In any case, bond interest could still be met through asset liquidation regardless of the surplus situation.

dividends that were charged to surplus. Without the surplus, could these dividends have been paid? From a standpoint of financial ability the surplus has little bearing upon the matter but legally the dividends could not have been paid without the surplus except as liquidating dividends. In reality, these were liquidating dividends, as will be demonstrated in Chapter 5. These two large steel companies paid 65 per cent of all the depression dividends tabulated in Table 12. In each case payments to common were reduced more than 80 per cent and payments to preferred were reduced equally as much. The amounts paid are substantial and impressive but the amounts omitted are even more impressive.

It will be observed from Table 12 that a number of automobile producers and machinery manufacturers paid depression dividends of several million dollars each. Without extended discussion the tabulation in Table 13 demonstrates that in most cases the dividends paid were a small fraction of the earnings reinvested during the twenties, that generally a much greater amount of the profits were lost than materialized as cash dividends, and that these companies retained a generous portion of the profits of the twenties.

TABLE 13—RETAINED EARNINGS AND DEPRESSION DIVIDENDS OF SELECTED AUTOMOBILE AND MACHINERY MANUFACTURERS
(Amounts in thousands of dollars)

| Company | Retained Earnings Reported Prosperity Period | | Reported Depression Losses | Preferred and Common Dividends Depression Years |
|---|---|---|---|---|
| | Amount | Per Cent of Total Earnings | | |
| Hudson Motor Car Co. | $46,970 | 52 | $14,640 | $8,115 |
| Reo Motor Car Co. | 13,001 | 41 | 9,791 | 2,372 |
| Packard Motor Car Co. | 40,536 | 34 | 13,628 | 6,746 |
| Deere & Co. | 28,848 | 53 | 8,716 | 4,877 |
| Allis-Chalmers Manufacturing Co. | 7,084 | 22 | 2,390 | 1,976 |
| J. I. Case Co. | 12,487 | 52 | 5,163 | 2,817 |
| Motor Wheel Corp. | 5,893 | 35 | 1,637 | 839 |
| Fairbanks, Morse & Co. | 7,876 | 35 | 4,537 | 726 |

*Prosperity Retained Earnings and Depression Dividends*

The data presented in Tables 10, 11, 12, and 13 provide convincing proof that: (1) the corporations which paid most of the depression dividends operated profitably even during the poorest years and therefore did not draw upon accumulated surplus extensively in order to make the payments; (2) the corporations that found it necessary to charge dividends to surplus made drastic reductions in the dividend rates. Although the aggregate amount of dividends paid from surplus charges is large in many cases, when compared with earnings withheld during the twenties these payments seem quite inadequate to recompense the stockholder for his forbearance during the best years; (3) there is no apparent relation between earnings reinvested during the twenties and dividends paid during the early thirties; (4) in almost one-half the enterprises a much greater portion of the 1922–30 reinvested profits was lost during depression years than was paid to stockholders.

## CHAPTER 4

# INVESTMENT OF RETAINED EARNINGS

Thus far the observations relating to corporate income administration have been based upon analysis of the income accounts.

Although the conclusions drawn therefrom are of vital significance, it is necessary to examine the balance sheets in order to discover the real effect and nature of reinvested earnings. Sound financial policy may dictate the retention of a portion of the income in order to provide for future losses and unforeseen contingencies. In essence, this statement means that net income cannot be measured in short time segments and it is therefore necessary to assume that short period reports are overoptimistic and do not recognize or cannot measure certain long term influences which inevitably reduce reported profits. Plowed back earnings measured in short time intervals represent a semisuspense account pending further developments.

It must be clear that reported short period income is supported and measured by valid assets, and retained income is represented by asset increases or liability decreases. The productive process culminates in revenue supported by eventual cash collections and corporate management formulates the expansion, investment, and dividend policies designed to make effective use of the funds produced. An examination of balance sheets reveals the manner in which retained earnings and new capital are invested and provides further convincing evidence that reinvested earnings do not create a *fund* or *reserve* from which dividends can be paid during bad years.

Nineteen companies in this sample increased the rate of common dividend payments during the depression, while twenty-nine of the enterprises reduced depression dividends more than 70 per cent. Did these two groups of corporations invest prosperity earnings in a distinctly different way which influenced or led to the different depression records?

*Nineteen Companies that Increased Dividends in Depression Years*

The companies which continued profitable operations after 1930 and increased dividend disbursements were producers of necessary consumption goods with the exception of four industrial chemical manufacturers. The composition of this continuously profitable group, classified by industry, shows:

5 food processors
5 tobacco and beverage companies
3 retail merchandisers
2 can companies
4 industrial chemical companies

In theory, these companies are expected to feel cyclical influences to only a moderate degree and as a consequence are expected to distribute generous dividends compared to current income. The periodic revenue and net income for these companies show remarkable stability, but they retained more of the 1922–30 income than any other group.

Table 14 assembles the fifteen year financial history of the nineteen companies and shows how funds were invested during the best years and extent of the liquidation during depression years. During the prosperity decade these corporations retained $779,224,000 which is 42 per cent of their reported operating income.

New stock and bond capital in excess of retirements totals $115,655,000 and added to reported retained income provides $894,879,000 for corporate expansion. Cash and liquid securities absorbed 35.5 per cent of these funds, while 22 per cent was invested in inventories and receivables. Working capital thus represents 56.5 per cent of the expansion during the twenties, while investment in plant assets absorbed 40 per cent of the combined reinvested income and net new capital.[1] Details

[1] One might say the $505,980,000 working capital increase came entirely from the $779,224,000 reported retained earnings, and on that assumption 65 per cent of the earned surplus was thus invested in working capital and perhaps 35 per cent in plant assets. There is little merit to the ranking of sources, however, and the writer prefers to regard new capital funds and retained income as a homogeneous supply of capital for corporate expansion.

Note that these percentage figures are based upon reported retained earnings plus *net* new capital issues, whereas Table 14 is based upon retained earnings plus all new capital.

TABLE 14—SOURCES AND APPLICATION OF FUNDS
Nineteen Companies Paying Larger Dividends during the Depression than during Prosperity
(Amounts in thousands of dollars)

| Source or Application | Prosperity Period | | Depression Period | Recovery Period | |
|---|---|---|---|---|---|
| | Amounts | Per Cent of Total Funds | | Amounts | Per Cent of Total Funds |
| Available to common | $1,699,657 | | $ 483,658 | $483,628 | |
| Common dividends | 920,433 | * | 510,919 | 364,131 | † |
| Retained earnings reported | $ 779,224 | 72.8 | $ −27,261 | $119,497 | 77.9 |
| Surplus adjustments | 7,402 | 0.7 | −42,713 | −22,275 | −14.6 |
| Retained earnings adjusted | $ 786,626 | 73.5 | $ −69,974 | $ 97,222 | 63.3 |
| Plant asset liquidation (unexpended depreciation) | 359 | 0.1 | 45,726 | 19,028 | 12.4 |
| Available from operations | $ 786,985 | 73.6 | $ −24,248 | $116,250 | 75.7 |
| Stock issued | 216,184 | 20.2 | 16,167 | 34,990 | 22.8 |
| Long term debt issued | 66,840 | 6.2 | 1,099 | 2,237 | 1.5 |
| Total available for investment | $1,070,009 | 100.0 | $ −6,982 | $153,477 | 100.0 |
| INVESTED IN | | | | | |
| Working capital | | | | | |
| Cash | $ 121,720 | 11.4 | $ −38,209 | $ 9,100 | 5.9 |
| Liquid securities | 196,167 | 18.3 | −135,862 | 19,669 | 13.0 |
| Receivables | 42,311 | 4.0 | −19,770 | 6,169 | 4.0 |
| Inventories | 155,831 | 14.6 | 54,580 | 66,815 | 43.5 |
| Current liabilities | −10,052 | −0.9 | 23,327 | −45,610 | −29.7 |
| Working capital change | $ 505,980 | 47.3 | $−115,934 | $ 56,143 | 36.6 |
| Investment, related companies | 12,806 | 1.2 | 58,308 | −6,459 | −4.2 |
| Sundry assets | 21,288 | 2.0 | −29,460 | −1,531 | −1.0 |
| Intangible assets | 3,803 | 0.4 | 4,921 | 2,334 | 1.5 |
| Plant assets | 358,776 | 33.5 | 12,077 | 9,352 | 6.1 |
| Stock retired | 103,156 | 9.6 | 49,900 | 65,518 | 42.7 |
| Long term debt retired | 64,213 | 6.0 | 13,207 | 28,128 | 18.3 |
| Total invested | $1,070,022 | 100.0 | $ −6,981 | $153,485 | 100.0 |

* Represents 54 per cent of earnings available to common stock. † Represents 75 per cent of earnings available to common stock.

of the utilization of funds, including both retained earnings and new capital, are presented in Table 15 for these nineteen companies.

TABLE 15—UTILIZATION OF EARNINGS AND NEW CAPITAL DURING PROSPERITY PERIOD
Nineteen Companies that Increased Dividend Payments during Depression Years

| Company | Percentage Application of Funds | | | | | |
|---|---|---|---|---|---|---|
| | Total | Working Capital | Securities Investments | Plant Assets | Retirement of Senior Securities | Sundry |
| Hershey Chocolate Corp. | 100 | 14 | -0- | -4 | 90 | -0- |
| General Cigar Company, Inc. | 100 | 48 | -4 | 19 | 37 | -0- |
| F. W. Woolworth Co. | 100 | 21 | 23 | 30 | 7 | 19 |
| Loose-Wiles Biscuit Co. | 100 | 23 | -0- | 54 | 11 | 12 |
| Coca-Cola Co. | 100 | 32 | 3 | 3 | 62 | -0- |
| Borden Co. | 100 | 27 | -5 | 73 | 5 | -0- |
| Air Reduction Company, Inc. | 100 | 53 | 14 | 33 | -0- | -0- |
| J. C. Penney Co. | 100 | 72 | 2 | 25 | 1 | -0- |
| Pillsbury Flour Mills Co. | 100 | 16 | 5 | 62 | 15 | 2 |
| Ligget & Myers Tobacco Co. | 100 | 100 | -0- | -0- | -0- | -0- |
| Continental Can Company, Inc. | 100 | 50 | 5 | 53 | -0- | -8 |
| American Can Co. | 100 | 19 | 3 | 64 | 12 | 2 |
| Mathieson Alkali Works, Inc. | 100 | 12 | 10 | 92 | -0- | -14 |
| S. S. Kresge Co. | 100 | 19 | -0- | 84 | 4 | -7 |
| Allied Chemical & Dye Corp. | 100 | 91 | -17 | 16 | 10 | -0- |
| R. J. Reynolds Tobacco Co. | 100 | 59 | -4 | 8 | 37 | -0- |
| Quaker Oats Co. | 100 | 62 | -2 | 40 | -0- | -0- |
| Wm. Wrigley, Jr. Co. | 100 | 88 | -9 | 13 | 8 | -0- |
| Commercial Solvents Corp. | 100 | 95 | -0- | -0- | 10 | -5 |

There is no predominant characteristic of investing income among these companies. Ten concerns invested more than 50 per cent of new funds in working capital, seven companies invested more than 50 per cent in plant facilities, and the other two companies retired senior securities.

In the poorest years of the early thirties according to reported figures, these nineteen companies paid $27,261,000 of dividends in excess of earnings and when adjusted for direct surplus charges the earning deficiency is nearly $70,000,000. Plant assets were liquidated for 65 per cent of this deficiency through the process of "unexpended depreciation." Working capital, especially liquid assets, decreased substantially although inventories increased. It is interesting to note that the working

capital decrease is almost equal to retirement of outstanding stocks and bonds plus investments in nonliquid securities of other companies.[2]

### *Twenty-Nine Companies that Reduced Common Dividends More than 70 Per Cent*

The twenty-nine companies that reduced common dividend payments by more than 70 per cent during the poorest years operate in the following industries:

3 automobile manufacturers (smaller companies)
3 automobile equipment manufacturers
4 railway equipment manufacturers
7 machinery manufacturers
7 steel manufacturers
1 merchandiser
1 tobacco company
2 rubber companies
1 chemical producer

For the most part, companies in this category produce capital equipment or durable consumer goods. All except three of the companies reported substantial operating losses during the poorest years, but eighteen of these corporations retained more than 30 per cent of total net income reported during the decade of the twenties. As a group they retained 29 per cent of total income reported during the best years which should be ample to smooth the dividend distribution if that accomplishment is possible from surplus reserves created by retaining earnings. It is interesting to note that only two of these companies paid dividends through the poorest years in excess of 10 per cent of 1930 assets.

Table 16 assembles in gross aggregates the fifteen year financial history of twenty-five companies with poorest depression common dividend records compared to the late twenties

[2] Figures published by the New York Stock Exchange in February, 1934, reveal that 259 corporations with shares listed on the New York Stock Exchange had reacquired portions of their own stock during the 1931–33 period.

TABLE 16—SOURCES AND APPLICATION OF FUNDS
Twenty-Five Companies that Reduced Common Dividends More than 70 Per Cent
(Amounts in thousands of dollars)

| Source or Application | Prosperity Period | | Depression Period | Recovery Period | |
|---|---|---|---|---|---|
| | Amounts | Per Cent of Total Funds | | Amounts | Per Cent of Total Funds |
| Available to common | $1,451,575 | | $-400,490 | $123,969 | |
| Common dividends | 747,018 | * | 72,732 | 34,277 | † |
| Retained earnings reported | $ 704,557 | 37.8 | $-473,222 | $ 89,692 | 33.3 |
| Surplus adjustments | -84,911 | -4.6 | -135,032 | -11,598 | -4.3 |
| Retained earnings adjusted | $ 619,646 | 33.2 | $-608,254 | $ 78,094 | 29.0 |
| Plant asset liquidation (unexpended depreciation) | 4,723 | 0.3 | 142,844 | 23,169 | 8.6 |
| Available from operations | $ 624,369 | 33.5 | $-465,410 | $101,263 | 37.6 |
| Stock issued | 892,851 | 47.9 | 14,389 | 37,231 | 13.8 |
| Long term debt issued | 346,454 | 18.6 | 85,515 | 131,009 | 48.6 |
| Total available for investment | $1,863,674 | 100.0 | $-365,506 | $269,503 | 100.0 |
| INVESTED IN | | | | | |
| Working capital | | | | | |
| Cash | $ 66,096 | 3.5 | $ -83,058 | $ 71,633 | 26.6 |
| Liquid securities | -59,973 | -3.2 | -57,335 | -44,495 | -16.5 |
| Receivables | 77,851 | 4.2 | -141,886 | 134,351 | 49.9 |
| Inventories | 165,455 | 8.9 | -216,636 | 170,796 | 63.5 |
| Current liabilities | -67,632 | -3.6 | 159,517 | -145,441 | -54.0 |
| Working capital change | $ 181,813 | 9.8 | $-339,398 | $186,844 | 69.4 |
| Investment, related companies | 62,496 | 3.4 | 10,827 | -3,011 | -1.1 |
| Sundry assets | 15,329 | 0.8 | -42,286 | -9,441 | -3.5 |
| Intangible assets | 87,556 | 4.7 | -79,371 | 20,334 | 7.5 |
| Plant assets | 725,935 | 39.0 | -48,033 | 3,763 | 1.4 |
| Stock retired | 116,649 | 6.3 | 17,770 | 12,527 | 4.6 |
| Long term debt retired | 673,898 | 36.0 | 114,986 | 58,486 | 21.7 |
| Totals | $1,863,674 | 100.0 | $-365,505 | $269,502 | 100.0 |

* Represents 51 per cent of earnings available to common stock. † Represents 28 per cent of earnings available to common stock.

and shows how the funds accumulated during the good years were invested and calls attention to the sources that enabled them to meet earning deficiencies of the early thirties.[3]

During the prosperity decade these twenty-five corporations retained $704,557,000 which is 49 per cent of the income reported available to common stockholders and 30 per cent of the $2,374,264,000 net income of the period. New stocks and bonds were issued in total amount of $1,239,305,000 but $790,547,000 were retired during the decade leaving $448,-758,000 of new capital in addition to retained earnings. If one regards net new capital and retained earnings as homogeneous funds available for investment, they were invested 16 per cent in working capital, 63 per cent in plant assets, 5 per cent in securities of related companies, and 16 per cent in other assets.[4] If we exclude United States Steel, these poor depression payers invested their available funds of the best years, 21 per cent in working capital, 63 per cent in plant facilities, 6 per cent in securities of related companies, and 10 per cent in other assets.

Table 17 assembles the twenty-five companies by name and shows, by chief asset categories, how the earnings and new capital contributions of the profitable period were invested. It is difficult to discern any uniformity in investment policies. Ten of the companies invested the funds 25 per cent or more in working capital, seventeen of the enterprises invested more than 25 per cent of their funds in plant assets, and fourteen of the companies utilized more than 25 per cent in retirement of stocks and bonds.

### *Comparative Analysis*

Table 18 is designed to display the manner in which nineteen continuously profitable generous depression dividend paying companies invested prosperity accumulations compared to twenty-five companies that reduced depression common dividends

[3] American Car and Foundry, American Locomotive, National Acme, and Worthington Pump reduced depression dividends more than 70 per cent but are excluded because of 1922–30 operating losses.

United States Steel is included in this group and represents approximately one-half the total figure.

[4] These figures do not appear in Table 16 because gross new capital is there considered as available for investment.

TABLE 17—UTILIZATION OF EARNINGS AND NEW CAPITAL DURING PROSPERITY PERIOD
Twenty-Five Companies that Reduced Dividends More than 70 Per Cent

| Company | Percentage Application of Funds | | | | | |
|---|---|---|---|---|---|---|
| | Total | Working Capital | Securities Invest-ments | Plant Assets | Retirement of Senior Securities | Sundry |
| Hudson Motor Car Co. | 100 | 48 | -0- | 51 | -0- | 1 |
| Deere & Co. | 100 | 67 | -0- | 8 | 28 | -3 |
| Inland Steel Co. | 100 | 19 | 12 | 42 | 24 | 3 |
| Allis-Chalmers Manufacturing Co. | 100 | 24 | -0- | 34 | 34 | 8 |
| B. F. Goodrich Co. | 100 | 14 | -3 | 48 | 39 | 2 |
| Reo Motor Car Co. | 100 | 65 | 1 | 32 | 2 | -0- |
| Bethlehem Steel Co. | 100 | 7 | 1 | 55 | 35 | 2 |
| United States Steel Corp. | 100 | -3 | 1 | 24 | 76 | 2 |
| J. I. Case Co. | 100 | 102 | -3 | 3 | -0- | -2 |
| Motor Wheel Corp. | 100 | 13 | 14 | 25 | 47 | 1 |
| Packard Motor Car Co. | 100 | -11 | 3 | 41 | 70 | -3 |
| Hart, Schaffner & Marx | 100 | 28 | 35 | -0- | 33 | 4 |
| Fairbanks, Morse & Co. | 100 | 58 | -4 | 24 | 10 | 12 |
| New York Air Brake Co. | 100 | 27 | -0- | -0- | 60 | 13 |
| Consolidated Cigar Corp. | 100 | 42 | -0- | 22 | 36 | -0- |
| American Cyanamid & Chemical Corp. | 100 | 23 | -5 | 53 | 9 | 20 |
| Baldwin Locomotive Works | 100 | -47 | 32 | 99 | -0- | 16 |
| Chicago Pneumatic Tool Co. | 100 | -26 | 10 | 80 | 36 | -0- |
| Crucible Steel Co. of America | 100 | -17 | -1 | 60 | 54 | 4 |
| Gulf States Steel Corp. | 100 | 5 | 1 | 88 | 3 | 3 |
| Republic Steel Corp. | 100 | 13 | 9 | 75 | 3 | -0- |
| Wheeling Steel Corp. | 100 | 26 | -1 | 55 | 13 | 7 |
| United States Rubber Co. | 100 | -14 | 59 | -223 | 110 | 168 |
| Mullins Manufacturing Corp. | 100 | 36 | -8 | 68 | 4 | -0- |
| Spicer Manufacturing Corp. | 100 | -1 | -6 | 116 | 125 | -134 |

more than 70 per cent. There is considerable similarity of policy among these companies which had such divergent depression experiences. Forty-seven per cent of the depression payers invested more than one-half their retained earnings and new capital in working capital and likewise 16 per cent of the companies which made drastic reductions in depression dividends invested more than one-half their retained income in the same manner. Fifty-eight per cent of the generous dividend companies invested less than one-half the prosperity funds in plant assets, and 52 per cent of the concerns that reduced dividends invested less than one-half in plant facilities.

TABLE 18—COMPARISON OF FUNDAMENTAL UTILIZATION POLICIES

| Per Cent of Retained Earnings Invested | Application of Funds | | | | |
|---|---|---|---|---|---|
| | Working Capital | Security Investment | Plant Assets | Retirement of Securities | Sundry |
| Companies Increasing Dividends | | | | | |
| Less than 25 | 7 | 13 | 7 | 15 | 14 |
| 25–50 | 3 | -0- | 4 | 2 | -0- |
| 50–75 | 5 | -0- | 5 | 1 | -0- |
| More than 75 | 4 | -0- | 2 | 1 | -0- |
| Liquidated | -0- | 6 | 1 | -0- | 5 |
| Total companies | 19 | 19 | 19 | 19 | 19 |
| Companies Reducing Dividends More than 70 Per Cent | | | | | |
| Less than 25 | 8 | 14 | 7 | 11 | 20 |
| 25–50 | 6 | 2 | 6 | 8 | -0- |
| 50–75 | 3 | 1 | 6 | 4 | -0- |
| More than 75 | 1 | -0- | 5 | 2 | 1 |
| Liquidated | 7 | 8 | 1 | -0- | 4 |
| Total companies | 25 | 25 | 25 | 25 | 25 |

It is recognized that income and new capital invested in various assets may not be the most significant factor. A profitable company might invest equal portions of the net income in a variety of assets while a much less profitable company might utilize all of its earnings to strengthen working capital and still be in unhealthy condition due to inadequate earnings in the first place.

If we compare 1921 working capital and plant assets with working capital and plant assets at the peak of the best years, the statistical fault just referred to is eliminated and the net percentage increase or decrease in these two main asset categories is measured.[5] Tables 19 and 20 show investments in working capital and fixed assets made by the continuously generous dividend payers compared to the companies which greatly reduced depression dividends.

[5] Write-ups, write-downs, and other inconsistencies in valuing various assets, especially in the plant accounting, render these figures unreliable to an undetermined but small extent in most cases. Likewise, transfers of securities from a marketable classification to investment accounts may have some influence on the net changes.

**TABLE 19—CHANGES IN WORKING CAPITAL AND PLANT ASSETS, PROSPERITY PERIOD**
**Nineteen Companies that Increased Dividend Payments during Depression Years**
**(Amounts in thousands of dollars)**

| Company | Working Capital | | | | Plant Assets | | | |
|---|---|---|---|---|---|---|---|---|
| | 1921 | 1930* | Increase | | 1921 | 1930* | Increase or Decrease | |
| | | | Amount | Per Cent | | | Amount | Per Cent |
| Hershey Chocolate Corp. | $-2,544 | $ 4,619 | $ 7,613 | -0- | $27,478 | $ 8,977 | $-18,501 | d67 |
| General Cigar Company, Inc. | 14,224 | 25,900 | 11,676 | 82 | 1,937 | 6,510 | 4,573 | 236 |
| F. W. Woolworth Co. | 24,708 | 52,781 | 28,073 | 114 | 16,953 | 57,251 | 40,298 | 270 |
| Loose-Wiles Biscuit Co. | 5,754 | 7,966 | 2,212 | 38 | 12,989 | 18,287 | 5,298 | 41 |
| Coca-Cola Co. | 874 | 13,957 | 13,083 | 1,497 | 5,767 | 6,873 | 1,106 | 19 |
| Borden Co. | 8,562 | 42,968 | 34,406 | 402 | 22,152 | 114,355 | 92,203 | 416 |
| Air Reduction Company, Inc. | 3,307 | 16,659 | 13,352 | 404 | 4,956 | 13,304 | 8,348 | 168 |
| J. C. Penney Co. | 8,422 | 50,516 | 42,094 | 500 | 971 | 15,638 | 14,667 | 1,511 |
| Pillsbury Flour Mills Co. | 2,757 | 6,921 | 4,164 | 151 | 2,216 | 18,146 | 15,930 | 719 |
| Liggett & Myers Tobacco Co. | 56,683 | 158,390 | 101,707 | 179 | 12,021 | 11,662 | -359 | d3 |
| Continental Can Company, Inc. | 2,958 | 31,075 | 28,117 | 951 | 11,713 | 45,853 | 34,140 | 292 |
| American Can Co. | 29,736 | 41,699 | 11,963 | 40 | 95,873 | 136,844 | 40,971 | 43 |
| Mathieson Alkali Works, Inc. | 1,201 | 2,404 | 1,203 | 100 | 6,979 | 16,477 | 9,498 | 136 |
| S. S. Kresge Co. | 9,953 | 25,930 | 15,977 | 161 | 11,973 | 83,907 | 71,934 | 601 |
| Allied Chemical & Dye Corp. | 66,150 | 144,470 | 78,320 | 118 | 88,323 | 101,978 | 13,655 | 16 |
| R. J. Reynolds Tobacco Co. | 78,775 | 139,184 | 60,409 | 77 | 8,369 | 16,544 | 8,175 | 98 |
| Quaker Oats Co. | 12,708 | 28,006 | 15,298 | 120 | 19,695 | 19,255 | -440 | d2 |
| Wm. Wrigley, Jr. Co. | 9,591 | 38,550 | 28,959 | 302 | 7,415 | 11,804 | 4,389 | 59 |
| Commercial Solvents Corp. | 253 | 8,053 | 7,800 | 3,083 | 1,237 | 1,237 | -0- | -0- |

* Wm. Wrigley, Coca-Cola, and General Cigar, period closes 1931. Liggett & Myers and R. J. Reynolds, period closes 1932. J. C. Penney, period closes 1929.

TABLE 20—CHANGES IN WORKING CAPITAL AND PLANT ASSETS, PROSPERITY PERIOD
Twenty-Five Companies that Reduced Dividends More than 70 Per Cent
(Amounts in thousands of dollars)

| Company | Working Capital | | | | Plant Assets | | | |
|---|---|---|---|---|---|---|---|---|
| | 1921 | 1930* | Increase or Decrease | | 1921 | 1930* | Increase or Decrease | |
| | | | Amount | Per Cent | | | Amount | Per Cent |
| Hudson Motor Car Co. | $ 2,962 | $ 25,608 | $ 22,646 | 765 | $ 9,059 | $ 33,276 | $ 24,217 | 267 |
| Deere & Co. | 58,803 | 63,045 | 4,242 | 7 | 19,298 | 22,143 | 2,845 | 15 |
| Inland Steel Co. | 13,652 | 26,104 | 12,452 | 91 | 34,527 | 62,670 | 28,143 | 82 |
| Allis-Chalmers Manufacturing Co. | 11,830 | 19,761 | 7,931 | 67 | 9,951 | 13,193 | 3,242 | 33 |
| B. F. Goodrich Co. | 48,618 | 58,920 | 10,302 | 21 | 32,116 | 67,600 | 35,484 | 110 |
| Reo Motor Car Co. | 10,552 | 20,198 | 9,646 | 91 | 5,922 | 10,689 | 4,767 | 80 |
| Bethlehem Steel Co. | 87,748 | 119,421 | 31,673 | 36 | 238,286 | 502,154 | 263,868 | 111 |
| United States Steel Corp. | 485,183 | 469,500 | −15,693 | −3 | 1,644,795 | 1,677,327 | 32,532 | 2 |
| J. I. Case Co. | 14,197 | 36,526 | 22,329 | 157 | 12,339 | 12,966 | 567 | 5 |
| Motor Wheel Corp. | 3,530 | 4,604 | 1,074 | 30 | 4,918 | 7,052 | 2,134 | 43 |
| Packard Motor Car Co. | 32,360 | 28,637 | −3,723 | −12 | 21,597 | 35,911 | 14,314 | 66 |
| Hart, Schaffner & Marx | 10,410 | 14,011 | 3,601 | 35 | 576 | 388 | −238 | −41 |
| Fairbanks, Morse & Co. | 11,830 | 19,761 | 7,931 | 67 | 9,951 | 13,193 | 3,242 | 33 |
| New York Air Brake Co. | 5,699 | 1,922 | −3,777 | −66 | 13,946 | 9,462 | −4,484 | −32 |
| Consolidated Cigar Corp. | 3,608 | 17,326 | 13,718 | 380 | 810 | 3,151 | 2,341 | 289 |
| American Cyanamid & Chemical Corp. | 1,969 | 18,614 | 16,645 | 845 | 4,242 | 42,535 | 38,293 | 903 |
| Baldwin Locomotive Works | 30,630 | 22,091 | −8,539 | −28 | 27,080 | 52,880 | 25,800 | 95 |
| Chicago Pneumatic Tool Co. | 8,335 | 7,665 | −670 | −8 | 8,922 | 10,967 | 2,045 | 23 |
| Crucible Steel Co. of America | 26,121 | 23,194 | −2,927 | −11 | 81,815 | 92,273 | 10,458 | 13 |
| Gulf States Steel Corp. | 2,225 | 2,964 | 739 | 33 | 13,441 | 25,979 | 12,538 | 93 |
| Republic Steel Corp. | 15,180 | 41,381 | 26,201 | 173 | 81,754 | 230,020 | 148,266 | 181 |
| Wheeling Steel Corp. | 22,743 | 33,052 | 10,309 | 45 | 54,478 | 76,584 | 22,106 | 41 |
| United States Rubber Co. | 83,724 | 79,448 | −4,276 | −5 | 169,657 | 101,384 | −68,273 | −40 |
| Mullins Manufacturing Corp. | 648 | 1,799 | 1,151 | 178 | 2,380 | 4,578 | 2,198 | 92 |
| Spicer Manufacturing Corp. | 3,596 | 3,880 | 284 | 8 | 3,807 | 7,885 | 4,078 | 107 |

* Hudson Motor Car, B. F. Goodrich, Reo Motor Car, and United States Rubber, period ends 1929. Consolidated Cigar, period ends 1931.

There is considerable evidence that the continuously profitable companies tended to increase working capital more and plant assets relatively less than companies that reduced dividends and generally reported depression losses. Whether this procedure caused the depression records or influenced their respective experiences is an entirely different matter. The first named group undoubtedly requires much less investment in plant facilities and probably requires considerably more investment in inventories. A condensed summary of the record appears in Table 21.

All of the continuously profitable companies increased working capital by large amounts. While many companies that reduced dividends drastically show large increases in working capital during the best years, many of them added little to the working capital and in 24 per cent of the cases it was reduced during the best years. Many of these concerns actually had no good years and therefore could not exercise much choice in the selection of investment media. The investment in plant assets is very similar between the two groups. Most of the companies made tremendously large investments in the plants, while several in each group reduced the book value of plant properties.

TABLE 21—DISTRIBUTION OF COMPANIES BY PERCENTAGE INCREASE IN WORKING CAPITAL AND PLANT ASSETS, PROSPERITY PERIOD

| Per Cent Increase | Working Capital | Plant Assets |
|---|---|---|
| | Number of Companies | Number of Companies |
| Companies Increasing Dividends | | |
| More than 100 | 15 | 9 |
| 50–100 | 2 | 2 |
| Less than 50 | 2 | 5 |
| Liquidated | –0– | 3 |
| Total Companies | 19 | 19 |
| Companies Reducing Dividends More than 70 Per Cent | | |
| More than 100 | 6 | 7 |
| 50–100 | 4 | 6 |
| Less than 50 | 8 | 9 |
| Liquidated | 7 | 3 |
| Total Companies | 25 | 25 |

*Twenty-Four Companies that Paid Substantial Depression Dividends in Excess of Earnings*

Attention is now directed to the remarkable record of twenty-four outstanding corporations (33 per cent of the sample) that paid cash dividends during the depression in spite of inadequate earnings or actual operating losses. How was the income of the best years invested in such a manner as to provide a "fund" or "reserve" from which depression dividends were paid? In Table 22 the companies that paid dividends requiring substantial charges to surplus are arranged by industry groups and within the groups in order of dividend maintenance.

During the decade of the twenties the twenty-four companies under observation had varying degrees of successful operation and some retained much and others retained little of the net income. In most cases the earnings were reinvested in all the asset categories or were used to retire outstanding debt and stock issues. In a few instances certain assets were selected as an investment reservoir, especially in the inventories. Plant equipment absorbed more of the retained income than any other asset, 75 per cent of the companies investing from 20 per cent to 55 per cent of the 1922–30 retained income in plant facilities.

There is little indication that the manner of investing earnings in the prosperous decade accounts for the depression records. Ability to pay dividends is dependent upon continued earnings and a company could reinvest all of the income made during a cyclical upswing in either working capital or plant facilities and still pay little if any dividends during a depression if there is inadequate revenue. If expanded plant facilities prove to be needed and can be operated profitably during recessions, a surplus reserve represented by such investment is a source of financial strength. On the contrary, if plants are idle during periods of slack business, the surplus reserve thus invested is a millstone. As long as a concern can produce revenue which recovers something more than out-of-pocket costs it can continue dividends and at the same time keep the working capital position healthy. If revenue is inadequate to meet the operating expenditures, it is almost a foregone conclusion that cash and marketable securities will prove inadequate to meet the occasion.

**Table 22—Percentage Investment of Retained Earnings and New Capital Issues, Prosperity Period Twenty-Four Companies Paying Depression Dividends Substantially in Excess of Current Earnings, Classified by Industry**

| Industry | Application of Funds | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Cash | Liquid Securities | Receivables | Inventories | Current Liabilities | Security Investments | Plant Assets | Capital Issues | Sundry |
| **Machinery manufacturing** | | | | | | | | | |
| Otis Elevator Co. | 16 | 1 | 18 | 18 | –7 | 20 | 32 | –0– | –0– |
| International Harvester Co. | 17 | 2 | 69 | –20 | –4 | 4 | 30 | –0– | 1 |
| Deere & Company | 5 | –0– | 91 | –25 | –3 | –3 | 8 | 28 | –0– |
| **Tire and rubber** | | | | | | | | | |
| Goodyear Tire & Rubber Co. | 20 | –5 | 11 | 30 | –8 | –21 | 41 | 44 | –12 |
| Firestone Tire & Rubber Co. | 21 | –0– | 4 | 25 | 14 | 5 | 26 | 3 | 2 |
| B. F. Goodrich Co. | 11 | –0– | 19 | 22 | –38 | –3 | 48 | 38 | 3 |
| **Electrical equipment** | | | | | | | | | |
| Westinghouse Electric & Manufacturing Co. | 13 | 1 | 12 | –9 | –3 | 36 | 22 | 33 | –5 |
| General Electric Co. | 47 | –11 | –6 | 1 | –7 | 60 | –10 | 17 | 9 |
| **Automobile** | | | | | | | | | |
| Chrysler Corp. | 21 | –1 | 7 | 18 | –8 | 5 | 42 | 16 | –0– |
| General Motors Corp. | 13 | 5 | 1 | 4 | –0– | 24 | 23 | 25 | 5 |
| Nash-Kelvinator Corp. | 1 | 48 | 1 | 2 | –1 | –0– | 7 | 43 | –0– |
| Packard Motor Car Co. | –1 | 24 | –0– | –27 | –6 | 3 | 41 | 70 | –4 |
| Mack Trucks, Inc. | –0– | –0– | 24 | 13 | –2 | 1 | 22 | 40 | 2 |
| Hudson Motor Car Co. | 7 | 26 | 6 | 21 | –13 | –0– | 51 | –0– | 2 |
| Timken Roller Bearing Co. | 1 | 39 | 4 | 4 | –0– | 6 | 37 | 6 | 3 |
| **Iron and steel** | | | | | | | | | |
| Bethlehem Steel Corp. | 2 | –2 | 2 | 7 | –3 | 1 | 55 | 36 | 2 |
| United States Steel Corp. | 1 | –10 | –3 | 14 | –4 | 1 | 24 | 76 | 1 |
| American Car and Foundry Co.* | –41 | –11 | –32 | –33 | –0– | –0– | –1 | –0– | –0– |
| **Merchandising** | | | | | | | | | |
| J. C. Penney Co. | 11 | –4 | 5 | 74 | –13 | 3 | 25 | 1 | –2 |
| Sears, Roebuck & Co. | –1 | 6 | –13 | 9 | 3 | 1 | 54 | 36 | 5 |
| California Packing Corp. | 1 | –0– | 16 | 28 | –28 | 35 | 38 | –0– | 10 |
| **Tobacco** | | | | | | | | | |
| General Cigar Company, Inc. | 4 | 8 | –0– | 31 | 4 | –4 | 19 | 37 | 1 |
| R. J. Reynolds Tobacco Co. | 32 | 14 | –0– | 13 | –0– | –4 | 9 | 37 | –1 |
| American Tobacco Co. | 29 | –0– | 3 | 29 | –3 | 21 | 9 | 11 | 1 |

* Net liquidation during the period.

## Chapter 5

# ASSET LIQUIDATION AND EARNING DEFICIENCIES

How did specific corporations meet their depression losses? It is in large measure nonsensical to say that surplus was drawn upon because surplus is a balancing figure on the equity side of the balance sheet even though it may represent earnings reinvested in some form. In this chapter the sampled corporations are divided into three groups in order to observe the process of asset liquidation during the depression years.

Seventeen companies (approximately 25 per cent of sample) paid dividends materially in excess of depression earnings.[1] Eighteen companies (25 per cent of the sample) paid dividends material in amount, after reporting operating losses. Ten concerns in this sample earned very little even during the best years and dividend payments were negligible, but how were the operating losses financed? Of the remaining twenty-seven companies in the sample, fifteen increased dividend payments during the poorest years but earned the requirements in full; ten reported net income during the depression but dividends were reduced sufficiently to stay within the income; and two companies had nominal losses and paid nominal dividends.

### *Seventeen Companies Paying Depression Dividends Substantially in Excess of Earnings*

During the poorest years a number of outstanding companies paid dividends considerably in excess of the reported income. Compared to total income retained during the decade of the twenties the disbursements were relatively small in most cases, but in immediate dollars the amounts appear impressive. How were surplus reserves invested and what assets were liqui-

[1] Companies are deemed to have paid a significant amount of dividends in excess of net income when common and preferred payments amount to $1,000,000, and if the disbursements exceed reported income available by more than 10 per cent. Companies in Table 22 paid dividends of more than $4,500,000, hence the difference in number of companies.

dated in order to meet the deficiencies? In condensed form the answers are presented in Tables 23, 24, and 25. For those interested in details of representative company performances, attention is directed to Appendix III A.

Table 23 shows in aggregates the asset expansion and liquidation through the 1922–33 cycle. Observe that percentagewise the asset structure does not differ greatly at any point

**TABLE 23—ASSET EXPANSION AND LIQUIDATION, 1921–33**
Seventeen Companies Paying Depression Dividends
Substantially in Excess of Earnings
(Amounts in thousands of dollars)

| Source or Application of Funds | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 117,960 | 19 | $ 381,275 | 34 | $ 205,123 | 24 | $-176,152 |
| Marketable securities | 71,460 | 12 | 145,898 | 13 | 151,295 | 18 | 5,397 |
| Receivables | 195,309 | 32 | 207,730 | 18 | 120,276 | 14 | -87,454 |
| Inventories | 396,452 | 65 | 598,098 | 53 | 517,857 | 60 | -80,241 |
| Total current assets | $ 781,184 | 128 | $1,332,998 | 118 | $ 994,553 | 115 | $-338,445 |
| Current liabilities | 170,332 | 28 | 199,934 | 18 | 131,244 | 15 | -68,690 |
| Net working capital | $ 610,850 | 46 | $1,133,062 | 49 | $ 863,310 | 45 | $-269,752 |
| Investments | 134,348 | 10 | 327,352 | 13 | 275,705 | 15 | -51,647 |
| Sundry assets | 11,264 | 1 | 21,781 | 1 | 16,180 | 1 | -5,601 |
| Intangible assets | 197,722 | 15 | 105,788 | 7 | 117,578 | 6 | 11,790 |
| Plant assets | 362,514 | 28 | 701,095 | 30 | 616,120 | 33 | -23,817 |
| Total | $1,316,695 | 100 | $2,289,079 | 100 | $1,888,893 | 100 | $-339,027 |
| Unexpended depreciation | | | | | | | 61,158 |
| Total liquidation | | | | | | | $ 400,185 |
| New security issues | | | | | | | 774 |
| Total deficiency | | | | | | | $ 400,959 |
| Intangible assets written off | | | | | | | 26,574 |
| Adjusted earning deficiency | | | | | | | $ 374,385* |
| Surplus reserves | $ 316,737 | | $ 978,912 | | $ 574,195 | | $-404,717 |
| Add: American Tobacco Company payment for brand names charged to surplus | | | | | 36,749 | | |
| | | | | | $ 610,944 | | $-367,968 |
| Losses reported | | | | | 23,180 | | |
| Dividends and interest | | | | | 155,402 | | |
| Write-downs and adjustments | | | | | 189,386 | | -367,968 |
| | | | | | $ 978,912 | | |
| Capital stock revaluations and stock dividends, net | | | | | | | 6,417 |
| | | | | | | | $ 374,385 |

* Earning deficiency adjusted, depression period, $374,385,000.
Earning deficiency reported, depression period, 205,799,000.
Retained earnings reported, prosperity period, 844,424,000.
Retained earnings adjusted, prosperity period, 865,823,000.

in the cycle. It should be noted also that much of the $404,717,000 decrease in surplus reserves is a result of write-offs and adjustments and does not appear because of dividend payments.

Table 24 shows the frequency and extent of asset liquida-

TABLE 24—EXTENT OF ASSET LIQUIDATION, DEPRESSION PERIOD
Seventeen Companies Paying Depression Dividends
Substantially in Excess of Reported Income

| Percentage Liquidation | Per Cent of Companies | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Cash | Liquid Securities | Receivables | Inventories | Total Current Assets | Current Liabilities | Net Working Capital | Investments | Plant Assets |
| 0– 9.9 | 12 | 23 | 6 | -0- | 12 | 6 | 17 | 12 | 47 |
| 10–19.9 | 6 | -0- | 12 | 24 | 24 | 17 | 17 | 18 | 35 |
| 20–29.9 | 12 | -0- | 12 | 6 | 24 | 12 | 30 | 6 | * |
| 30–39.9 | 6 | 12 | 23 | 29 | 28 | 17 | 24 | 6 | * |
| 40–49.9 | 6 | 6 | 6 | 12 | 12 | -0- | 12 | 18 | * |
| 50–59.9 | 23 | -0- | 12 | 6 | -0- | 12 | -0- | -0- | * |
| 60–69.9 | 6 | -0- | 23 | 6 | -0- | 12 | -0- | -0- | * |
| 70–79.9 | -0- | -0- | -0- | -0- | -0- | 12 | -0- | -0- | * |
| 80–89.9 | 12 | 6 | -0- | -0- | -0- | -0- | -0- | -0- | * |
| 90–99.9 | -0- | 12 | -0- | -0- | -0- | -0- | -0- | -0- | * |
| (Increases) | 17 | 41 | 6 | 17 | -0- | 12 | -0- | 40 | 6 |
| Totals | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 88 |

* 12 per cent of the companies wrote down plant assets substantially.

tion during the poorest years.[3] The liquidation rarely reached 40 per cent of the 1930 amounts while the degree of liquidation in the various assets followed no particular pattern among the companies.

It is interesting to note that marketable securities and investments in related companies actually increased in 41 per cent of the cases during the poorest years. This record is exactly as it should be. Security prices are lower during the depression years than at any other time and if securities are to be held at all they should be purchased at just such times. Inventories and receivables are the assets most often liquidated during the depression according to data presented in Table 24.

It is hardly feasible to show by percentages or other relatives exact portions of the earning deficiency provided by liquidating various assets. It is possible to state, in general, how earning deficiencies were met in each case, and in Table 25 each company is listed by name showing in order of magnitude

[3] The degree of asset liquidation is computed by dividing the 1931–33 or 1931–34 decrease by the 1930 year-end asset figures.

the three assets liquidated which provided most of the funds to meet the earning deficiency. In most cases the first two assets named account for a very large part of the total liquidation. Inventories provided much of the earning deficiency in more than two-thirds of the cases, while liquid assets supplied an important part of the deficiency in 35 per cent of the cases. Receivables were liquidated by most companies, and plant assets made an important contribution in at least 70 per cent of the cases.

TABLE 25—ASSETS LIQUIDATED TO GREATEST EXTENT, DEPRESSION PERIOD
Seventeen Companies Paying Depression Dividends Substantially in Excess of Reported Earnings

| Company | Assets Arranged According to Degree of Liquidation | | |
|---|---|---|---|
| | 1 | 2 | 3 |
| May Department Stores Co. | Inventories | Receivables | Plant assets |
| J. C. Penney Co. | Inventories | New issues | Plant assets |
| Sears, Roebuck & Co. | Receivables | Inventories | Plant assets |
| American Tobacco Co. | Liquid assets | New issues | Plant assets |
| R. J. Reynolds Tobacco Co. | Liquid assets | New issues | Receivables |
| General Cigar Company, Inc. | Inventories | Plant assets | Receivables |
| Otis Elevator Co. | Inventories | Receivables | Plant assets |
| General Electric Co. | Liquid assets | Inventories | Receivables |
| Chrysler Corp. | Plant assets | Inventories | Receivables |
| Firestone Tire & Rubber Co. | Liquid assets | Inventories | Sundry |
| Inland Steel Co. | New issues | Liquid assets | Investments |
| Nash-Kelvinator Corp. | Liquid assets | Plant assets | Receivables |
| Packard Motor Car Co. | Plant assets | Inventories | Liquid assets |
| Timken Roller Bearing Co. | Plant assets | Inventories | Sundry |
| Union Carbide & Carbon Corp. | Liquid assets | Inventories | Receivables |
| American Brake Shoe & Foundry Co. | Receivables | Plant assets | Liquid assets |
| Electric Storage Battery Co. | Receivables | Inventories | Plant assets |

### *Eighteen Companies that Paid Dividends after Losses*

When the record of these eighteen companies that paid at least \$1,000,000 of depression dividends (after reporting depression losses) is assembled in aggregate, we find approximately \$700,000,000 of prosperity profits reinvested, 30 per cent going into working capital and 68 per cent invested in plant assets. It should be noted that the working capital increases took place in receivables and inventories entirely while

liquid assets shifted slightly from marketable securities to cash. In percentage terms, the asset structure of 1921 and 1930 year ends is almost identical. (See Table 26.)

TABLE 26—ASSET EXPANSION AND LIQUIDATION, 1921–33
Eighteen Companies Paying Substantial Depression Dividends after Operating Losses
(Amounts in thousands of dollars)

| Source or Application of Funds | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 194,710 | 17 | $ 265,764 | 20 | $ 183,149 | 18 | $ −82,615 |
| Marketable securities | 224,020 | 20 | 154,363 | 11 | 148,499 | 14 | −5,864 |
| Receivables | 291,397 | 26 | 461,629 | 34 | 245,863 | 24 | −215,766 |
| Inventories | 648,489 | 58 | 774,948 | 58 | 592,379 | 53 | −182,569 |
| Total current assets | $1,358,615 | 121 | $1,656,704 | 123 | $1,169,894 | 114 | −486,814 |
| Current liabilities | 236,106 | 21 | 309,371 | 23 | 142,988 | 14 | $−166,383 |
| Net working capital | $1,122,511 | 30 | $1,347,333 | 30 | $1,026,907 | 26 | $−320,431 |
| Investments | 66,061 | 2 | 144,164 | 3 | 120,492 | 3 | −23,672 |
| Sundry assets | 71,727 | 2 | 86,056 | 2 | 27,662 | 1 | −58,394 |
| Intangible assets | 84,717 | 2 | 78,204 | 1 | 24,286 | 1 | −53,918 |
| Plant assets | 2,426,450 | 64 | 2,903,144 | 64 | 2,721,637 | 69 | −88,101 |
| Total | $3,772,005 | 100 | $4,558,901 | 100 | $3,920,984 | 100 | |
| Unexpended depreciation | | | | | | | 93,406 |
| Total liquidation | | | | | | | $ 637,922 |
| New security issues | | | | | | | −13,654 |
| Total deficiency | | | | | | | $ 624,268 |
| Write-offs against capital stock | | | | | | | 13,424 |
| Adjusted earning deficiency | | | | | | | $ 610,844* |
| Surplus reserves | $1,245,870 | | $1,502,796 | | $ 940,307 | | −562,489 |
| Losses | | | | | 208,185 | | |
| Interest and dividends | | | | | 300,653 | | |
| Write-downs and adjustments | | | | | 53,651 | | 562,489 |
| | | | | | $1,502,796 | | |
| Capital stock revaluations | | | | | | | 47,995 |
| | | | | | | | $ 610,844 |

* Earning deficiency adjusted, depression period, $610,844,000.
Earning deficiency reported, depression period, 489,803,000.
Retained earnings reported, prosperity period, 708,613,000.
Retained earnings adjusted, prosperity period, 695,343,000.

In aggregates, the depression record shows that every class of asset was liquidated in order to meet the earning deficiency. Receivables and inventories provided perhaps 50 per cent of the funds for the depression deficiency after liquidating the accounts payable, and all other assets contributed to supply the balance.

In each individual case and in aggregates, it is obvious that prosperity earnings generally were reinvested in all classes of assets but primarily in receivables, inventories, and plant. During depression periods when sales decline it is natural and inevitable that physical inventory needs will decline and unit costs will be lower, hence inventory investment is liquidated. Receivables likewise are collected or written off as uncollectible and the collection process always provides some funds to meet an operating deficiency. In like manner, plant improvements and expansion during the upswing make productive capacity excessive during the slump and further plant expansion and even full maintenance is not desirable. Depreciation must be recognized even during the lean years when selling prices do not recover all the costs of operation and it is therefore very probable that plant assets will be liquidated in the process of meeting the earning deficiency.

The degree of asset liquidation made by this group of durable goods manufacturers that operated at a loss during depression years is summarized in Table 27. Only 20 per cent

TABLE 27—EXTENT OF ASSET LIQUIDATION, DEPRESSION PERIOD
Eighteen Companies Paying Substantial Depression Dividends after Operating Losses

| Percentage Liquidation | Per Cent of Companies | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Cash | Liquid Securities | Receivables | Inventories | Total Current Assets | Current Liabilities | Net Working Capital | Investments | Plant Assets |
| 0– 9.9 | -0- | 5 | -0- | -0- | -0- | -0- | 5 | -0- | 39 |
| 10–19.9 | 11 | -0- | 6 | 17 | 6 | -0- | 11 | -0- | 28 |
| 20–29.9 | -0- | 11 | -0- | 28 | 28 | 22 | 29 | 6 | -0- |
| 30–39.9 | 11 | -0- | 28 | 22 | 33 | 11 | 28 | -0- | 5 |
| 40–49.9 | 22 | 4 | 33 | 11 | 17 | 17 | 11 | -0- | -0- |
| 50–59.9 | -0- | -0- | 17 | -0- | 11 | 6 | -0- | 11 | -0- |
| 60–69.9 | -0- | -0- | 11 | 17 | 5 | 11 | 5 | -0- | -0- |
| 70–79.9 | 17 | 6 | -0- | -0- | -0- | 11 | -0- | -0- | -0- |
| 80–89.9 | 6 | -0- | 5 | -0- | -0- | 17 | 6 | -0- | -0- |
| 90–99.9 | -0- | 11 | -0- | -0- | -0- | 5 | -0- | -0- | -0- |
| Write-downs and small amounts | -0- | 24 | -0- | -0- | -0- | -0- | -0- | 33 | 28 |
| (Increases) | 33 | 39 | -0- | 5 | -0- | -0- | 5 | 50 | -0- |
| Totals | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |

of the companies reduced the cash account more than 40 per cent and one-third of these depression losers actually increased their cash balances. Marketable securities were liquidated in degree much less than cash. Only four of the eighteen companies

reduced marketable securities as much as 30 per cent while 39 per cent of the enterprises added to their investment in securities.

In more than 60 per cent of the cases receivables decreased between 30 and 50 per cent and in a third of the cases the shrinkage was more than 50 per cent. The inventory shrinkage was more than 50 per cent in only two cases, but in absolute amounts inventory liquidation was substantial in most instances. Current liabilities were reduced to a minimum during the depression, one-half the concerns reducing current liabilities more than 50 per cent while all except one company reduced current payables at least 20 per cent. Investments in nonmarketable securities were liquidated in very few cases as one might suspect. Plant assets were liquidated by practically every company and this liquidation supplied an important part of the earning deficiency but did not absorb a large fraction of total plant costs.[8] For representative company records see Appendix III B.

Shifts in asset classifications, such as marketable securities to investments, and revaluations and write-downs, make it difficult to specify that liquidation of particular assets provided a certain percentage of the earning deficiency. By observation, some indication can be given as to which assets provided most of the earning deficiency, however, and in Table 28 the companies are listed by name, showing the three assets which provided most of the deficiency.

Receivables, inventories, and plant assets were liquidated most frequently and proved to be the greatest source of "surplus liquidation," while 44 per cent of the companies relied upon a balance of cash and marketable securities to supply much of the depression deficiency.

### *Ten Companies that Paid No Depression Dividends*

The analysis of thirty-five companies just examined shows that profitable companies invested earnings in a variety of ways,

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[8] There is some reason to assume that depreciation charges were reduced below a reasonable rate and that plant liquidation was in reality more extensive than reported figures suggest.

TABLE 28—ASSETS LIQUIDATED TO GREATEST EXTENT, DEPRESSION PERIOD
Eighteen Companies Paying Substantial Depression
Dividends after Operating Losses

| Company | Assets Arranged According to Degree of Liquidation | | |
|---|---|---|---|
| | 1 | 2 | 3 |
| American Car & Foundry Co. | Receivables | Inventories | Investments |
| American Locomotive Co. | Liquid assets | Inventories | Receivables |
| Allis-Chalmers Manufacturing Co. | Receivables | Inventories | Liquid assets |
| J. I. Case Co. | Receivables | Inventories | Plant assets |
| Deere & Co. | Receivables | Plant assets | Inventories |
| International Harvester Co. | Receivables | Plant assets | None |
| Worthington Pump & Machinery Corp. | Liquid assets | Receivables | Inventories |
| Westinghouse Electric & Manufacturing Co. | Receivables | Inventories | Liquid assets |
| B. F. Goodrich Co. | Inventories | Receivables | Plant assets |
| Bethlehem Steel Co. | Inventories | Receivables | Plant assets |
| United States Steel Corp. | Liquid assets | Inventories | Plant assets |
| Hudson Motor Car Co. | Liquid assets | Inventories | Plant assets |
| Mack Trucks, Inc. | Liquid assets | Inventories | Plant assets |
| Reo Motor Car Co. | Liquid assets | Inventories | Plant assets |
| California Packing Corp. | Liquid assets | Receivables | Inventories |
| Consolidated Cigar Corp. | Inventories | Receivables | None |
| Crucible Steel Co. of America | Inventories | Plant assets | Liquid assets |
| Wheeling Steel Corp. | Liquid assets | Inventories | Plant assets |

chiefly in receivables, inventories, and plant facilities, and that earning deficiencies were met by liquidating these same assets.

Ten companies included in the present sample paid no dividends of any consequence during the depression and in most cases operated at a loss. The railway equipment, steel, machinery, and other manufacturers in this category had a generally poor 1922–30 earning record and in most cases the dividends paid even in the best years were comparatively small amounts. These ten companies as a whole operated at a loss for fifteen years, yet they are still important companies in their respective industries. How is it possible to operate below cost for long periods of time and what sort of surplus reserves did these concerns have in order to withstand the rigorous early thirties after a series of operating losses through the twenties?

We find little difference between the asset structure of the ten poor companies and the more profitable companies already

examined. A deficit arose in a number of cases, to be sure, but the assets were little affected by the deficit as such and the particular companies were able to continue operations without any surplus. The limited amount of 1922–30 expansion occurred chiefly in plant assets, although inventories and cash show extensive increases. The financial records of representative companies are summarized in Appendix III C.

All assets were liquidated in varying degree during the depression, a feature observed in performances of the more profitable concerns. The asset structure at terminal points of the cycle is proportionately very similar as shown by the aggregate financial summary in Table 29.

TABLE 29—ASSET EXPANSION AND LIQUIDATION, 1921–33
Ten Companies Having Small Prosperity Earnings and Paying Only Nominal Depression Dividends
(Amounts in thousands of dollars)

| Source or Application of Funds | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 19,108 | 12 | $ 43,376 | 23 | $ 29,662 | 25 | $ −13,714 |
| Marketable securities | 27,115 | 17 | 12,432 | 6 | 2,151 | 2 | −10,284 |
| Receivables | 69,924 | 44 | 68,958 | 36 | 35,172 | 30 | −33,786 |
| Inventories | 124,453 | 79 | 136,542 | 72 | 83,334 | 71 | −53,208 |
| Total current assets | $240,602 | 152 | $261,308 | 137 | $150,315 | 128 | $−110,994 |
| Current liabilities | 82,755 | 52 | 71,027 | 37 | 33,517 | 28 | −37,510 |
| Net working capital | $157,845 | 29 | $190,281 | 23 | $116,802 | 19 | $ −73,482 |
| Investments | 21,418 | 4 | 63,492 | 8 | 65,562 | 11 | 2,069 |
| Sundry assets | 16,043 | 3 | 16,003 | 2 | 12,283 | 2 | −3,720 |
| Intangible assets | 23,222 | 4 | 78,832 | 10 | 7,774 | 1 | −71,058 |
| Plant assets | 333,797 | 60 | 485,236 | 57 | 398,345 | 67 | −26,324 |
| Total | $552,326 | 100 | $833,844 | 100 | $600,764 | 100 | |
| Unexpended depreciation | | | | | | | 60,567 |
| Total liquidation | | | | | | | $ 233,082 |
| Intangible assets written off† | | | | | | | 58,925 |
| Capital issues retired | | | | | | | 64,099 |
| Adjusted earning deficiency | | | | | | | $ 110,058* |
| Surplus reserves | $108,881 | | $157,013 | | $ 50,645 | | −106,368 |
| Losses | | | | | 36,768 | | |
| Interest and dividends | | | | | 34,389 | | |
| Write-downs and adjustments | | | | | 35,211 | | |
| | | | | | $157,013 | | 106,368 |
| Capital stock revaluations and adjustments to capital surplus | | | | | | | 3,690 |
| | | | | | | | $ 110,058 |

* Earning deficiency adjusted, depression period, $110,058,000.
Earning deficiency reported, depression period, 71,102,000.
Retained earnings reported, prosperity period, 69,925,000.
Retained earnings adjusted, prosperity period, 6,141,000.

† See Appendix III C, United States Rubber Company.

Table 30 shows the frequency and degree of liquidation in each asset. Forty per cent of the companies increased the cash accounts during the poorest years and only 20 per cent of the group reduced cash 50 per cent or more. Among these ten companies with poorest dividend records, liquid securities were not important in the asset structure in 60 per cent of the cases, but where a company owned such securities they were liquidated during the depression. Receivables and inventories were liquidated from 20 to 50 per cent, a record very similar to other

TABLE 30—EXTENT OF ASSET LIQUIDATION, DEPRESSION PERIOD
Ten Companies Having Small Prosperity Earnings and Paying Only Nominal Depression Dividends

| Percentage Liquidation | Per Cent of Companies | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Cash | Liquid Securities | Receivables | Inventories | Total Current Assets | Current Liabilities | Net Working Capital | Investments | Plant Assets |
| 0– 9.9 | -0- | -0- | 10 | -0- | -0- | -0- | -0- | 10 | 40 |
| 10–19.9 | -0- | -0- | 20 | 10 | 20 | 20 | 20 | -0- | 20 |
| 20–29.9 | 10 | -0- | 10 | 30 | 10 | 10 | 10 | -0- | 10 |
| 30–39.9 | 10 | -0- | -0- | 20 | 10 | -0- | -0- | 10 | -0- |
| 40–49.9 | 20 | -0- | 10 | 10 | 30 | 10 | 30 | 10 | -0- |
| 50–59.9 | 10 | -0- | 10 | 10 | 30 | 10 | 10 | 10 | -0- |
| 60–69.9 | 10 | -0- | 30 | 10 | -0- | 10 | 10 | -0- | -0- |
| 70–79.9 | -0- | 20 | -0- | -0- | -0- | 20 | 10 | -0- | -0- |
| 80–89.9 | -0- | -0- | -0- | -0- | -0- | 10 | -0- | -0- | -0- |
| 90–99.9 | -0- | 20 | -0- | -0- | -0- | -0- | -0- | -0- | -0- |
| Very small liquidation | -0- | 60 | -0- | -0- | -0- | -0- | -0- | 30 | -0- |
| Write-downs | -0- | -0- | -0- | -0- | -0- | -0- | -0- | -0- | 30 |
| (Increases) | 40 | -0- | 10 | 10 | -0- | 10 | 10 | 30 | -0- |
| Totals | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |

groups observed. Investments in securities of related companies were of little importance but in several instances increased during the poorest years,[4] and plant asset liquidation was substantial in amount in most cases.

In Table 31 each company is listed by name, showing in order of magnitude the three assets which provided most of the earning deficiency. Receivables, inventories, and plant facilities were liquidated most often to provide an important portion of the funds to meet the earning deficiency of the early thirties, while cash and marketable securities were the most important source of funds in 30 per cent of the cases.

[4] Liquid securities may have been reclassified as "investments" because of drastic declines in market values and restricted marketability.

TABLE 31—ASSETS LIQUIDATED TO GREATEST EXTENT, DEPRESSION PERIOD
Ten Companies Having Small Prosperity Earnings and Paying Only Nominal Depression Dividends

| Company | Assets Arranged According to Degree of Liquidation | | |
|---|---|---|---|
| | 1 | 2 | 3 |
| Gulf States Steel Corp. | Plant assets | Inventories | Receivables |
| American Cyanamid & Chemical Corp. | Inventories | Sundry assets | Receivables |
| Baldwin Locomotive Works | Liquid assets | Receivables | Inventories |
| Lima Locomotive Works, Inc. | Liquid assets | Plant assets | None |
| New York Air Brake Co. | Plant assets | Inventories | Receivables |
| Chicago Pneumatic Tool Co. | Inventories | Plant assets | Receivables |
| National Acme Co. | Liquid assets | Inventories | Plant assets |
| United States Tire Co. | Inventories | Receivables | Plant assets |
| Republic Steel Corp. | Plant assets | Inventories | Liquid assets |
| Mullins Manufacturing Corp. | Inventories | Receivables | None |

### *Summary*

The detailed investigation of asset accumulation and liquidation indicates that a particular company may invest the surplus reserves in many combinations or fashions and that depression earning deficiencies may be met by liquidating whatever assets economic forces permit or make feasible. In general, however, when companies are operating profitably a considerable portion of the reported income necessarily remains invested in receivables, inventories, and plant facilities as well as in the more liquid assets. The same economic forces which cause these assets to increase during the best years cause a liquidation and shrinkage of those values during recessions.

In Table 32 the degree and nature of asset liquidation during the depression years is summarized in a way designed to compare general tendencies of three groups. There appear to be very minor differences in asset liquidation among the companies with such different profit and dividend records.

TABLE 32—PERCENTAGE DISTRIBUTION OF COMPANIES BY ASSETS LIQUIDATED TO GREATEST EXTENT, THREE GROUPS OF COMPANIES

| Assets Liquidated | Per Cent of Companies in Which Asset Liquidation Was One of Three Most Important Sources of Funds | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Seventeen Companies Paying Depression Dividends Substantially in Excess of Reported Income | | | Eighteen Companies Paying Substantial Depression Dividends after Operating Losses | | | Ten Companies Having Small Prosperity Earnings and Paying Only Nominal Depression Dividends | | |
| | 1 | 2 | 3 | 1 | 2 | 3 | 1 | 2 | 3 |
| Liquid assets | 35 | 5 | 12 | 45 | -0- | 25 | 30 | -0- | 10 |
| Receivables | 18 | 12 | 35 | 33 | 28 | 6 | -0- | 30 | 48 |
| Inventories | 24 | 47 | -0- | 22 | 55 | 19 | 40 | 40 | 13 |
| Plant assets | 18 | 18 | 35 | -0- | 17 | 50 | 30 | 20 | 25 |
| Sundry | 5 | 18 | 18 | -0- | -0- | -0- | -0- | 10 | -0- |
| | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |

## Chapter 6

# CONCLUSIONS

The merits of saving for a rainy day and the effectiveness of corporate surplus in meeting financial requirements of depression periods have been widely publicized and accepted, but in practice it is questionable whether corporate reserves assure wage and dividend payments during the poor years. It is possible that a period of disinvesting, dishoarding, and real capital liquidation made possible in large part by surplus accumulation, may result in less employment of all factors of production during recession periods and hence the payment of less wages and dividends.

Increased sales volume and a rising price level during the upswing of a business cycle require additional investments in receivables, inventory, and plant assets. The saving is therefore semiautomatic, and it is doubtful if corporate management exercises deliberate choice in the administration of much of the reported annual income. Day to day expenditures must be made to maintain the flow of revenue, and at periodic time intervals dividend payments are considered. On such occasions the cash balance and liquid position are likely to be of much greater importance than accrued net income and a large surplus balance.

Since surplus is ordinarily invested in increased productive facilities there is no *fund* which can be drawn upon for dividend payments when revenue is inadequate to meet operating expenditures. Decline in business activity forces a reduction and liquidation in receivables, inventory, and plant facilities. Selling prices do not recover all the costs of operation during the recession periods, due chiefly to uncollectible accounts, declines in inventory values, and depreciation of plant facilities that cannot be operated to efficient capacity. Management is forced to discharge laborers, reduce wage payments, sell the existing inventories at lower prices, and reduce expenditures for plant maintenance. Proceeds from sales may more than recover out of pocket expenditures during the liquidating period and still

fail to cover the total costs of production. This phenomenon explains how losses are reported while liquid position is maintained or improved and while the surplus balance declines.

If depression period operating revenue exceeds current expenditures by virtue of the fact that prosperity profits were used to build up a surplus reserve invested in receivables, inventories, and plant equipment, then these productive facilities may be liquidated at prices below cost and the so-called surplus may be utilized to pay dividends to stockholders and thus disburse income that was withheld during profitable years. Neither managers nor stockholders would knowingly subscribe to such a policy.

The purpose of this study has been to show the extent to which depression dividends were paid from surplus reserves created during the twenties, to show how those reserves were reinvested, and how depression losses were met.

The following observations seem warranted:

1. Many of our industrial corporations financed large expansion programs during the twenties by reinvesting profits and paying scanty dividends.

2. Depression dividends were paid by companies that continued to operate profitably, and only limited amounts were paid in excess of earnings. Very moderate dividends were paid by companies reporting losses, with a few outstanding exceptions.

3. Nineteen of the companies (26.4 per cent of the sample) increased common dividend payments during the poorest years, but these corporations continued profitable operations throughout the depression period; charges to surplus were the exception; and in aggregate amount a very small proportion of their dividends came from surplus.

4. The corporations that found it necessary to charge dividends to surplus made drastic reductions in the dividend rates and although the aggregate amount of dividends paid from surplus is large in a number of cases, these payments are small when compared with earnings withheld during the twenties.

5. There is no apparent relation between earnings reinvested during the twenties and dividends paid during the early thirties.

6. Almost one-half of the companies lost a much greater portion of the 1922–30 withheld earnings than they paid to stockholders in cash dividends during the depression years.

7. Corporate surplus resulting from reinvested profits is not a cash fund but is reflected in a cross section of all the assets, and property acquired from retained earnings cannot be distinguished from assets acquired through the sale of stocks or bonds or by other methods of financing.

8. In general, industrial corporations retained some 40 per cent of the 1922–30 net income and this they invested chiefly in inventories, receivables, and plant facilities, with moderate increases in cash and marketable securities. The data demonstrate that these same assets were liquidated during the poorest years and this forced liquidation probably accounts for most of the reported losses as well as providing funds to meet the operating deficiencies.

# APPENDIXES

# APPENDIX I

## Industrial Classification of the Sample Showing Name of Company and Assets Invested by Each Company

| Industry | Assets Invested (Amounts in thousands of dollars) | | |
|---|---|---|---|
| | 1921 | 1928 | 1936 |
| *Railway equipment manufacture* | | | |
| American Brake Shoe and Foundry Co. | $ 23,194 | $ 32,408 | $ 30,608 |
| American Car and Foundry Co.* | 136,663 | 121,058 | 96,584 |
| American Locomotive Co.* | 85,630 | 108,093 | 56,856 |
| Baldwin Locomotive Works* | 81,931 | 69,403 | 73,979 |
| Lima Locomotive Works, Inc. | 16,115 | 13,773 | 9,034 |
| New York Air Brake Co. | 14,457 | 16,253 | 12,872 |
| Total in sample (6) | $ 357,990 | $ 360,988 | $ 279,933 |
| *Machinery manufacture* | | | |
| Allis-Chalmers Manufacturing Co.* | 60,432 | 63,547 | 79,003 |
| Chicago Pneumatic Tool Co. | 18,696 | 19,312 | 20,038 |
| J. I. Case Co. | 35,179 | 42,636 | 42,250 |
| Deere & Co.* | 87,445 | 91,983 | 94,424 |
| Fairbanks, Morse & Co. | 26,265 | 39,039 | 30,840 |
| International Harvester Co.* | 266,672 | 346,120 | 398,874 |
| National Acme Co. | 33,481 | 10,679 | 5,446 |
| Otis Elevator Co. | 27,167 | 50,403 | 39,849 |
| Owens-Illinois Glass Co. | 34,130 | 32,898 | 72,975 |
| Pittsburgh Plate Glass Co.* | 64,388 | 96,124 | 114,439 |
| Worthington Pump & Machinery Corp. | 32,915 | 28,692 | 23,715 |
| Total in sample (11) | $ 686,770 | $ 821,433 | $ 921,853 |
| *Electrical equipment* | | | |
| General Electric Co.* | 337,010 | 460,455 | 378,869 |
| Westinghouse Electric & Manufacturing Co.* | 167,070 | 233,690 | 203,735 |
| Total in sample (2) | $ 504,080 | $ 694,145 | $ 582,604 |
| *Rubber manufacture* | | | |
| Firestone Tire & Rubber Co.* | 66,211 | 110,127 | 147,015 |
| B. F. Goodrich Co.* | 88,801 | 116,224 | 139,092 |
| Goodyear Tire & Rubber Co.* | 163,085 | 207,666 | 196,029 |
| United States Rubber Co.* | 323,653 | 284,206 | 172,365 |
| Total in sample (4) | $ 641,750 | $ 718,223 | $ 654,501 |

APPENDIX I—Cont'd.

| Industry | Assets Invested (Amounts in thousands of dollars) | | |
|---|---|---|---|
| | 1921 | 1928 | 1936 |
| *Iron and steel manufacture* | | | |
| Bethlehem Steel Co.* | $ 336,422 | $ 643,356 | $ 656,576 |
| Crucible Steel Co. of America* | 113,463 | 118,385 | 110,524 |
| Gulf States Steel Corp. | 16,747 | 25,383 | 30,742 |
| Inland Steel Co.* | 49,856 | 95,176 | 137,644 |
| Republic Steel Corp.* | 106,813 | 151,435 | 343,950 |
| United States Steel Corp.* | 2,339,143 | 2,442,030 | 1,863,977 |
| Wheeling Steel Corp.* | 87,474 | 125,098 | 118,825 |
| Total in sample (7) | $3,079,918 | $3,600,863 | $3,262,238 |
| *Automobile manufacture* | | | |
| Chrysler Corp.* | 56,515 | 194,172 | 210,676 |
| General Motors Corp.* | 413,705 | 1,030,162 | 1,196,435 |
| Hudson Motor Car Co. | 15,189 | 68,237 | 42,779 |
| Mack Trucks, Inc. | 29,250 | 68,497 | 46,038 |
| Nash-Kelvinator Corp. | 26,111 | 63,479 | 36,544 |
| Packard Motor Car Co. | 58,759 | 75,177 | 58,030 |
| Reo Motor Car Co. | 18,932 | 37,297 | 11,212 |
| Total in sample (7) | $ 618,461 | $1,537,021 | $1,601,714 |
| *Automobile equipment manufacture* | | | |
| Electric Storage Battery Co. | 41,029 | 47,084 | 38,713 |
| Motor Wheel Corp. | 9,244 | 15,409 | 12,452 |
| Mullins Manufacturing Corp. | 4,281 | 7,898 | 3,563 |
| Spicer Manufacturing Corp. | 15,834 | 13,416 | 9,863 |
| Timken Roller Bearing Co. | 19,105 | 45,523 | 46,745 |
| Total in sample (5) | $ 89,493 | $ 129,330 | $ 111,336 |
| *Chemical manufacture* | | | |
| Air Reduction Company, Inc. | 9,952 | 24,429 | 41,315 |
| Allied Chemical & Dye Corp.* | 205,355 | 262,242 | 225,046 |
| American Cyanamid & Chemical Corp. | 16,812 | 23,461 | 62,858 |
| Commercial Solvents Corp. | 2,240 | 10,097 | 20,225 |
| E. I. du Pont de Nemours & Co.* | 245,339 | 419,204 | 622,556 |
| Mathieson Alkali Works, Inc. | 11,709 | 17,923 | 26,205 |
| Union Carbide & Carbon Corp.* | 200,042 | 236,837 | 290,313 |
| Total in sample (7) | $ 691,449 | $ 994,193 | $1,288,518 |
| *Metal container* | | | |
| American Can Co.* | 134,995 | 183,262 | 211,374 |
| Continental Can Company, Inc.* | 26,763 | 63,161 | 104,734 |
| Total in sample (2) | $ 161,758 | $ 246,423 | $ 316,108 |

APPENDIX I—Cont'd.

| Industry | Assets Invested (Amounts in thousands of dollars) | | |
|---|---|---|---|
| | 1921 | 1928 | 1936 |
| *Food processing* | | | |
| Borden Co.* | $ 60,215 | $ 119,284 | $ 123,894 |
| California Packing Corp. | 44,299 | 55,950 | 56,334 |
| Corn Products Refining Co.* | 133,623 | 121,327 | 119,912 |
| Hershey Chocolate Corp. | 43,265 | 22,084 | 25,635 |
| Loose-Wiles Biscuit Co. | 20,089 | 26,203 | 28,890 |
| National Biscuit Co.* | 83,188 | 120,842 | 123,979 |
| Pillsbury Flour Mills Co. | 10,992 | 28,626 | 27,245 |
| Quaker Oats Co. | 40,322 | 61,566 | 63,518 |
| Total in sample (8) | $ 435,993 | $ 555,882 | $ 569,407 |
| *Mercantile merchandising* | | | |
| Hart, Schaffner & Marx | 24,885 | 29,557 | 9,005 |
| S. S. Kresge Co.* | 31,081 | 100,657 | 120,382 |
| May Department Stores Co. | 45,412 | 73,744 | 60,937 |
| J. C. Penney Co. | 11,433 | 49,106 | 82,327 |
| Sears, Roebuck & Co.* | 184,819 | 209,282 | 275,292 |
| F. W. Woolworth Co.* | 102,918 | 153,516 | 201,224 |
| Total in sample (6) | $ 400,548 | $ 615,862 | $ 749,167 |
| *Tobacco and beverage* | | | |
| American Tobacco Co.* | 190,462 | 221,206 | 255,412 |
| Coca-Cola Co. | 35,510 | 47,185 | 78,406 |
| Consolidated Cigar Corp. | 12,034 | 31,214 | 16,097 |
| General Cigar Company, Inc. | 39,041 | 31,307 | 25,372 |
| Liggett & Myers Tobacco Co.* | 137,244 | 181,403 | 175,979 |
| R. J. Reynolds Tobacco Co.* | 104,488 | 156,260 | 146,605 |
| Wm. Wrigley, Jr. Co. | 29,804 | 52,435 | 60,713 |
| Total in sample (7) | $ 548,583 | $ 621,390 | $ 758,584 |

* Among America's two hundred largest industrials, most of them being mentioned by Berle and Means in *The Modern Corporation and Private Property.*

# APPENDIX II

## Some Problems in Income Determination

The necessity for interpretation of surplus adjustments will be emphasized if we observe some actual surplus accounting. In 1921 Sears Roebuck reported a loss of $16,000,000 although a profit of over $8,000,000 on the sale of real estate was credited direct to surplus. In 1933 Woolworth reported total income of some $28,000,000. In addition a profit of $1,970,561.13 was made on the sale of securities and this profit was credited direct to surplus. In 1931 American Cyanamid reduced the stated value of common stock $39,035,000 thus creating a capital surplus. Among other things the plant assets were written down $19,995,672, patents and process written down $12,268,468, and investments in securities decreased by $3,502,470. In 1929 Commercial Solvents charged to earned surplus $1,725,240 which represented the undepreciated value of plant assets, and on order of the board of directors wrote off against surplus the cost of stock acquired in Commercial Pigments Corporation. In 1934 this stock was sold at a figure far above cost and $4,525,510 was credited to surplus.

In 1926 and again in 1934 Inland Steel dismantled plants and charged the respective unrecovered costs of $1,201,000 and $1,030,000 to surplus. In 1932 Consolidated Cigar reported profits of $114,000 but made a charge to surplus of $1,244,000 due to a reduction in inventory value of leaf tobacco. In 1935 United States Steel reduced plant assets by about $85,000,000 as a result of obsolescence and reduced the plant properties another $182,000,000 through a credit to a general reserve for amortization of property investment valuations.

It seems important to emphasize that these adjustments are a part of the business operations and affect fortunes of the stockholder equally as much as other profits or expenses. It is also important to differentiate between surplus entries arising from a receipt or disbursement of cash, those which affect subsequent

income accounts through arbitrary revaluation of assets, and those which are nominal in nature, such as goodwill write-offs when the goodwill was orginally stock discount if correctly interpreted.

In order to show how depression losses and dividends were met, it is necessary to distinguish between expenses which require a current expenditure and those which represent consumption of assets acquired in previous periods. The most important of these expenses that require no current expenditure is depreciation.

### *Unexpended Depreciation*

Much of the 1922–30 retained income was invested in plant assets, as shown in Chapter 4. The process of liquidating plant assets and consequent depreciation charges inherent in reporting such liquidation gives rise to much confusion, of which the following excerpts are typical.

In *The Annalist* of January 14, 1938, Alexander Sachs presents data which show that durable goods industries financed their recovery primarily from depreciation.[1] A few weeks later a subscriber to *The Annalist* professed inability to understand the process, expressing his doubts as follows:

> As a new subscriber I have been mystified by some remarkable statements in an article on page 35 of your Jan. 14 issue. The author, Alexander Sachs, discusses "How Industry Financed Recovery" and states "Depreciation remained the chief source of funds." To a layman, even one with considerable business experience, this sounds incomprehensible, if not fantastic. Perhaps you will help me to obtain a clarification.
>
> Dr. Sachs lists the three main purposes for which industry has required funds. For these purposes real money has been clearly necessary. Yet he says this money was obtained from "depreciation." How can an arbitrary bookkeeping entry provide real money or directly affect the physical wealth of a corporation in any way? [2]

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[1] A. Sachs, "Summary of a Comprehensive Financial Analysis of the Causes of the Slump," *The Annalist*, January 14, 1938, p. 35.

[2] C. Pennington, "Depreciation as a Source of Financing," *The Annalist*, February 25, 1938, p. 292.

In explaining this phenomenon, Alexander Sachs says:

> In sum, depreciation is one constituent of appropriated income and is just as much "real money" as the net income itself. It is, in fact, that portion of the income which is segregated so as to serve a dual function: accounting-wise, it is an allocation for wear and tear of the equipment over its life; management-wise—that is, from the standpoint of the active manager of the business who is concerned with conserving his property and utilizing the wear and tear allocation for maintaining the dynamic efficiency of the whole plant or business—it is a source of funds for physical reinvestment and for other purposes of capital formation.[3]

Mr. Pennington accepted the explanation of the depreciation charge as a source of funds in the following language:

> The fact remains that if the companies listed by Dr. Sachs had elected, in any year, to charge off ten million more as depreciation than they did charge off, they would not thereby have added one dime to the total of their funds available for plant expansion or for increasing inventories or receivables. Therefore, to speak of depreciation as a source of funds, however correct as a step in accounting practice, has no significance in a discussion of fundamentals.[4]

One must admit that the explanation given is not very convincing even if correct. Unexpended depreciation is an unfortunate expression intended to describe a process of plant liquidation which recognizes the expense of plant use without a corresponding expenditure for plant assets within the period. Investment in plant can be liquidated just as can government bonds, inventories, or any other asset. The sale of government bonds will provide funds, whether sold above or below cost. A stock of merchandise can be liquidated at a price below cost without replenishment of the inventory and presumably this process would provide liquid funds available for any purpose whatsoever. It is not the expense or cost of merchandise that produces the funds, however, but the *revenue* which arises when the merchandise is sold.

Plant assets are liquidated in a manner quite like inventory liquidation except for differences in periodicity. When sales are

[3] A. Sachs, *The Annalist*, February 25, 1938, p. 292.
[4] Pennington, *op. cit.*

made at a profit, the cost elements of merchandise, store supplies, advertising, rent, salaries, and other assets are liquidated and replaced by cash or receivables in amount sufficient to result in a net asset increase. When sales are made at a price which does not recover *all* costs, certain assets are liquidated as usual in the sales process, but a net asset decrease results—otherwise the sale price would not be below cost. It is not possible to determine *which* cost factor is not recovered in the selling price, even though the ranking of costs is a common practice. Most expense items are computed by actual count of units used and there is little question concerning the amount of such expense or in what operating period it belongs. It is not feasible to measure the inches of floor space worn from a building or the molecules of wear on the roof of a factory, yet the cost of these items must be recovered in the selling price. Assets received measure the revenue volume and depreciation accounting in no way can affect the assets already received.

A moment of reflection will convince even the most casual observer that the harvest has already been made and the "pumpkins are in the cellar" before depreciation is entered on the books. After a year of operations and at the close of a fiscal period, all cash is in the bank, all uncollected accounts receivable on the books, the inventory on the shelves, and the buildings, machinery, and equipment on their foundations. A bookkeeping entry which debits Depreciation Expense and credits Allowance for Depreciation changes the situation not one iota. No fund results which can be directed to plant maintenance or to any other use. While depreciation is a very real expense, it produces no fund or stream of current assets ready for reinvestment any more than the labor expense, rent expense, or delivery expense. Assets available for investment come from revenue produced or from income, and measure the amount of revenue or income. To be sure, there may be a liquidation of fixed assets through operations, but it does not arise from the depreciation charge. The process would proceed exactly in the same way and the amount of liquidation would be precisely the same whether or not any depreciation charge is made—unless one wants to argue that short run costs as computed set selling prices and hence determine profits. Unexpended depreciation is, therefore,

the estimated cost of plant assets liquidated and included in the sales price of merchandise sold during the year.

Computation of unexpended depreciation from reports to stockholders is in many cases fraught with inaccuracies and must of necessity rest at times upon arbitrary assumptions due to lack of information. If $8,000 is charged to depreciation and a $5,000 expenditure is capitalized for plant expansion, $3,000 may be looked upon as unexpended depreciation. In a more realistic sense, wear and tear, obsolescence, and other factors entering the depreciation expense exceed the current replacement to physical assets and to that extent plant assets have been sold in the operating process. In very unusual cases reports to stockholders disclose both capital expenditures and depreciation expenses. In general, however, information is limited to the annual depreciation charge, allowance for depreciation, and plant asset totals. In a number of cases only the net plant asset total is given and in such circumstances unexpended depreciation is pure estimate and assumption.

Where accounting for plant assets follows some consistent principle it is possible to compute unexpended depreciation with a reasonable degree of satisfaction.[5] The unexpended

[5] If no units of equipment are discarded or revalued, the net change in plant assets plus depreciation charge represents capital outlay. If in 1934 plant assets are presented in this manner:

| Plant | | Allowance for Depreciation | |
|---|---|---|---|
| 400,000 | | | 100,000 |

and the 1934 depreciation charge is $50,000 and $30,000 is expended for new construction, the net plant asset decrease of $20,000 represents unexpended depreciation and could be discovered by mere observation of the accounts which would appear thus:

| Plant | | Allowance for Depreciation | |
|---|---|---|---|
| 400,000 | | | 100,000 |
| 30,000 | | | 50,000 |

The net decrease in balance sheet plant account under these conditions would be due to unexpended depreciation. If a unit which cost $20,000 and has a book value of $2,000 is disposed of with no scrap value, the net decrease in book value overstates unexpended depreciation to the extent of the $2,000 unrecovered cost. If charged to surplus the facts may be apparent and proper adjustment can be made, but in condensed reports the details of surplus analysis are seldom revealed. In event plant assets are disposed of at a gain over the undepreciated book figure and if the gain results from excessive depreciation, then any amounts recognized as unexpended depreciation have been overstated. To make this point clear,

depreciation figures in the Earnings and Dividends tables have a tendency to be overstated slightly, but the overstatement probably is negligible.[6]

*Surplus Reserve Adjustments*

Thus far complications suggested in relation to the measurement of year to year income and funds available for dividends have been confined to earned surplus adjustments and unexpended depreciation. Debits and credits to surplus, however, do not explain all the discrepancy between balance sheet changes in common stock equity and aggregate reported retained earnings plus or minus stock issued or retired. One practically despairs of preparing an accurate source and disposition of funds statement from reports to stockholders because of the *reserve* accounts and lack of information concerning changes therein. It is necessary in a historical study of retained earnings to classify reserve accounts into asset contras, liabilities, and proprietary reserves. The following discussion is intended to suggest the problem as

assume machine X cost $80,000 in 1930 and a depreciation rate is designed to recover the cost in four years with no scrap value. If no other expenditures were made, unexpended depreciation of $20,000 would be recorded each year. If at the end of four years the machine is sold for $25,000 it is clear that unexpended depreciation has been overstated. These details usually are not revealed in reports to stockholders, hence there may be more or less error in accepting net plant decreases as unexpended depreciation even after correcting for all visible surplus entries. The unexpended depreciation as presented is not presumed to be exact in amount but the margin of error is not great.

[6] In an effort to verify unexpended depreciation figures I addressed inquiries to a number of corporations and included a schedule designed to show the annual depreciation charge, plant expenditures, plant retirements, and amounts received from plant sales and salvage. The response was not satisfactory, but a number of officials suggested that the procedure just outlined would be reasonably accurate. A letter from Howard Berry, Vice-President and Treasurer of Mathieson Alkali Works, is typical.

"Starting with the Accumulated Depreciation Reserve at the beginning of the year; adding the Depreciation for the year as shown in the Analysis of Income Account and from that total deducting the accumulated Depreciation at the end of the year would give approximately the plant retirements charged against the depreciation reserve.

"This last figure mentioned added to the net increase in the Property Account shown by the Balance Sheet each year should give approximately the total outlay for plant.

"Of course, the foregoing does not take into consideration the net proceeds from the sale of scrap, etc., but this item is more or less negligible."

it was met and to indicate how the various accounts were interpreted.

Reserves were used by many institutions included in this survey and with few exceptions their function is to report uniform amounts of income each year in spite of all actual realities. Some of the common reserves appearing on the equity side of balance sheets are:

Reserve for Contingencies
Reserve for General Contingencies
Reserve for Taxes
Reserve for Investments
Sundry Reserves
General Reserves
Reserve for Insurance
Reserve for Depreciation and Obsolescence
Reserve for Expansion
Reserve for Improvements
Special Reserves
Reserve for Common Dividends
Reserve for Pensions
Reserve for Accident Compensation
Reserve for Collection Expense
Reserve for Losses in Closed Banks
Reserve forRetirement of Bonds
Reserve for Employee Compensation
Reserve for Inventory Losses
Reserve for Shrinkage in Receivables and Inventory
Reserve for Fire Loss
Reserve for Foreign Exchange
Operating Reserve
Reserve for Replacements
Reserve for Depreciation
Reserve for Relining and Rebuilding Furnaces
Reserve for Employee Benefits
Reserve for Capital Expenditures
Reserve for Working Capital
Reserve for Premium on Preferred Stock
Reserve for Redemption of Preferred Stock

One or more of these accounts were employed by nearly all companies and from time to time they were reclassified and combined. By title and general use most reserve accounts can be classified with fair accuracy especially if information is available concerning how the account is operated, but from condensed income reports and balance sheets a categorical treatment must be resorted to because of lack of information.

The most commonly used reserve for contingencies is universally regarded as surplus, but in many instances there was no way to be certain of its nature. In a few cases like the Otis Elevator report of 1925, a debit to surplus and credit to reserve for contingencies of $1,325,000 leaves no doubt in one's mind. In other cases the charges or credits to contingencies were buried in the operating expense section. In any event, book value of assets must increase or decrease by an amount equal to the change in reserve and there is little choice but to regard the contingency reserve as surplus. Accurate interpretation of changes based on reports to stockholders usually was impossible, since there is no way to know whether changes were a result of actual expenditures, revaluations, profit from exceptional sources, or a reversal of some entry which created the reserve. In the measurement of retained earnings, changes in the reserve for contingencies have been regarded as a correction of reported earnings.

It would be possible to enter into an extended discussion of each reserve account used and to point out the many interpretations which might be given to explain how the entries could affect reported earnings. In the measurement of earnings for one year periods, many charges are made to expense which require no expenditure. This does not deny the validity of the expense, but when net assets increase more than the reported retained earnings some adjustment must be made. Either the asset and liability changes must be denied or the reported income must be adjusted, and in this study (with limitations) the latter procedure is accepted as the situation most likely to approach reality. Reserve accounts appear as credit balances because debits were made to operating expense, income, or surplus. Where entries are purely voluntary and no outside creditor equity can possibly be read into the account, it usually represents segregated surplus at any balance sheet date.

Reserve for insurance is of limited application but it is one of the borderline type and will illustrate implications just made. The principle of self-insurance for fire, flood, tornado, and other hazards is well understood. Where distribution of the risk justifies self-insurance and where calculated on a scientific basis, the annual charge for insurance expense can be accepted as a legitimate charge to the periodic revenue, but the credit to reserve for insurance at any balance sheet date must represent losses provided for which have not occurred. In the final analysis, a charge to insurance premiums actually paid to secure protection is distinctly different from a charge to expense for self-insurance. Protection actually paid for is a real service since it substitutes a certain small cost for an uncertain possible great loss. The self-insurance expense is hardly an expense, because the self-insurer elects to take his own risk. If at the balance sheet date no losses have occurred, assets are greater than they would have been had insurance premiums actually been paid. When destruction results from some cause, the *loss* must and does come in that year. In essence, the self-insurer has fire, flood, tornado, or other similar *expenses* but not *insurance* expense. Annual income reports may be more uniform when self-estimated premiums are recorded as an expense, but it is another case of accounting technique designed to show uniform operating results which are in reality not uniform. In the treatment given, increases and decreases in the reserve for insurance, fire loss, and similar reserves were regarded as additions to or deductions from reported retained income.

It was not always possible to be certain of the nature of changes and adjustments in the reserve accounts and in most companies not a hint of explanation appeared in the reports. Large amounts and common accounts in most instances were interpreted with reasonable satisfaction. The lack of information contained in reports to stockholders and the apparently inconsistent and thoughtless manner in which the accounts are used proved to be annoying, but the utterly impossible tangles would form a very small part of the total earnings reported.

*Procedure Illustration*

The measurement of prosperity earnings retained and the amount of dividends paid from those retained earnings in subsequent years is not an easy task as already indicated. The procedure and technique of measuring retained earnings, their investment and liquidation, is better understood if we observe in detail the operating results of a particular company during the fifteen years. Hudson Motor Car Company is a purposely simple illustration as the surplus entries are not numerous and all represent outright expenses and the reserve for contingencies is easily understood.

Cash dividends paid, deducted from reported income available to common stockholders, is adjusted for the entries made directly in the surplus and reserve for contingency accounts, and combined with the new capital issued or retired gives the annual amount "Available for Investment." [7]

The schedule of Investment and Disinvestment shows precisely how the funds were invested during profitable years and which assets were liquidated to meet losses and pay dividends during the depression. The detailed figures of Hudson Motor Car Company show how all the data were assembled for each of the seventy-two companies.

[7] To the amount "Available for Investment" presented in the schedule of Operating Results, should be added "unexpended depreciation." In the tables unexpended depreciation is considered available for use, but is shown in the illustration in a manner designed to keep income sheet and balance sheet items clearly separated.

Hudson Motor Car Company
Operating Results, 1922–36
(Figures in thousands)

| Year | Available to Common | Common Dividends | Retained Earnings Reported | Surplus Adjustments | Contingency Reserve | Total Adjustments | Retained Earnings Adjusted | New Issues | Available for Investment |
|---|---|---|---|---|---|---|---|---|---|
| 1922 | $ 7,243 | $ 1,761 | $ 5,482 | $ 733* | –0– | $ 733 | $ 6,214 | $ 14 | $ 6,228 |
| 1923 | 8,004 | 3,601 | 4,403 | –232† | –0– | –232 | 4,171 | –0– | 4,171 |
| 1924 | 8,073 | 3,781 | 4,292 | –250‡ | 250 | –0– | 4,292 | –0– | 4,292 |
| 1925 | 21,378 | 4,975 | 16,403 | –230‡ | 51 | –179 | 16,225 | 125 | 16,350 |
| 1926 | 5,373 | 5,189 | 184 | –108† | –8 | –116 | 68 | –0– | 68 |
| 1927 | 14,431 | 6,918 | 7,513 | –150† | 150 | –0– | 7,513 | –0– | 7,513 |
| 1928 | 13,457 | 8,179 | 5,278 | –150† | 149 | –1 | 5,277 | –0– | 5,277 |
| 1929 | 11,595 | 8,180 | 3,415 | –300† | 594 | 294 | 3,709 | –0– | 3,709 |
| Totals | $ 89,554 | $42,584 | $ 46,970 | $ –687 | $ 1,186 | $ 499 | $ 47,469 | $ 139 | $ 47,608 |
| 1930 | 325 | 6,518 | –6,194 | –2,266§ | –306 | –2,572 | –8,766 | –626 | –9,392 |
| 1931 | –1,991 | 1,597 | –3,588 | –6,533‖ | 2,372 | –4,161 | –7,749 | –546 | –8,295 |
| 1932 | –5,429 | –0– | –5,429 | –3,031¶ | –2,019 | –5,050 | –10,479 | 871 | –9,608 |
| 1933 | –4,410 | –0– | –4,410 | –0– | 672 | 672 | –3,738 | –603 | –4,341 |
| 1934 | –3,239 | –0– | –3,239 | –0– | 6 | 6 | –3,233 | 263 | –2,970 |
| Totals | $–14,744 | $ 8,115 | $–22,860 | $–11,830 | $ 725 | $–11,105 | $–33,965 | $ –641 | $–34,606 |
| 1935 | 585 | –0– | 585 | 483 | –95 | 388 | 973 | 5,259 | 6,232 |
| 1936 | 3,306 | –0– | 3,306 | –0– | 83 | 83 | 3,389 | –1,900 | 1,489 |
| Totals | $ 3,891 | –0– | $ 3,891 | $ 483 | $ –12 | $ 471 | $ 4,362 | $3,359 | $ 7,721 |

* No explanation.
† Prior year taxes.
‡ Transferred to contingency reserve.
§ Special costs of tools and materials due to new models.

‖ Transferred to contingency reserve........$ 500,000
Shrinkage foreign subsidiaries............ 2,000,000
Special tool costs...................... 2,000,000
Special advertising costs ................ 1,400,000
Cost of plant rearrangement ............ 632,707
Total..............................$6,532,707

¶ Write-off of production facilities and rearrangement of plant due to reduced operations........$2,567,508
Loss on obsolete equipment............. 463,125
Total..............................$3,030,633

Hudson Motor Car Company
Investment and Disinvestment, 1922–29
(Figures in thousands)

| Item | 1921 | 1922 | 1923 | 1924 | 1925 | 1926 | 1927 | 1928 | 1929 | Total Prosperity Investment |
|---|---|---|---|---|---|---|---|---|---|---|
| Working capital | | | | | | | | | | |
| Cash | $ 1,290 | $ 7,327 | $ 5,354 | $ 6,877 | $ 6,715 | $ 4,463 | $ 5,286 | $ 6,015 | $ 4,760 | $ 3,470 |
| Government securities | –0– | –0– | 4,000 | 6,000 | 17,000 | 6,000 | 8,000 | 14,000 | 12,385 | 12,385 |
| Receivables | 1,041 | 2,883 | 602 | 2,607 | 5,069 | 1,912 | 3,564 | 5,007 | 3,862 | 2,821 |
| Inventories | 3,558 | 5,378 | 6,453 | 6,118 | 11,055 | 9,186 | 13,989 | 13,168 | 13,467 | 9,909 |
| Prepaids | –0– | –0– | –0– | –0– | –0– | –0– | –0– | –0– | –0– | –0– |
| Total current | $ 5,888 | $15,498 | $16,410 | $21,602 | $39,839 | $21,561 | $30,839 | $38,190 | $34,474 | $28,585 |
| Current liabilities | 2,926 | 6,044 | 4,726 | 6,551 | 14,705 | 7,341 | 10,796 | 12,076 | 8,865 | 5,939 |
| Net working capital | $ 2,962 | $ 9,454 | $11,684 | $15,051 | $25,135 | $14,221 | $20,043 | $26,114 | $25,608 | |
| Change | | 6,492 | 2,230 | 3,367 | 10,083 | −10,914 | 5,822 | 6,071 | −505 | $22,646 |
| Investments | $ 79 | $ 68 | $ 69 | $ 84 | $ 81 | $ 39 | $ 41 | $ 40 | $ 39 | |
| Change | | −11 | 1 | 15 | −3 | −42 | 2 | −1 | −1 | $ −40 |
| Deferred charges | $ 162 | $ 140 | $ 857 | $ 955 | $ 537 | $ 787 | $ 1,047 | $ 935 | $ 947 | |
| Change | | −22 | 717 | 98 | −418 | 250 | 260 | −112 | 12 | 785 |
| Plant assets | | $13,142 | $15,259 | $17,277 | $25,425 | $38,795 | $42,976 | $44,701 | $51,629 | |
| Allowance for depreciation | | 4,314 | 5,209 | 6,414 | 7,875 | 10,471 | 13,223 | 15,629 | 18,353 | |
| Net plant assets | $ 9,059 | $ 8,828 | $10,050 | $10,863 | $17,550 | $28,324 | $29,753 | $29,072 | $33,276 | |
| Change | | −231 | 1,222 | 813 | 6,687 | 10,774 | 1,429 | −680 | 4,204 | $24,217 |
| Net investment | | $ 6,228 | $ 4,170 | $ 4,293 | $16,349 | $ 68 | $ 7,513 | $ 5,278 | $ 3,710 | $47,608 |

Hudson Motor Car Company
Investment and Disinvestment, 1930–36
(Figures in thousands)

| Item | 1930 | 1931 | 1932 | 1933 | 1934 | Disinvestment 1930–34 | 1935 | 1936 | Investment 1935–36 |
|---|---|---|---|---|---|---|---|---|---|
| Working capital | | | | | | | | | |
| Cash | $ 4,953 | $ 1,841 | $ 2,110 | $ 2,335 | $ 2,576 | $ 2,184 | $ 9,584 | $10,038 | $ 7,462 |
| Government securities | 9,030 | 7,068 | 2,089 | 345 | –0– | 12,385 | –0– | 1,999 | 1,999 |
| Receivables | 4,306 | 1,364 | 853 | 361 | 745 | 3,117 | 1,810 | 1,731 | 986 |
| Inventories | 6,844 | 4,476 | 3,615 | 4,492 | 4,562 | 8,905 | 4,885 | 8,006 | 3,444 |
| Prepaids | –0– | –0– | –0– | –0– | 393 | –393 | 392 | 405 | 12 |
| Total current | $25,133 | $14,749 | $ 8,666 | $ 7,533 | $ 8,276 | $26,198 | $16,671 | $22,179 | $13,903 |
| Current liabilities | 5,301 | 3,590 | 2,200 | 4,461 | 6,138 | 2,727 | 6,704 | 9,794 | 3,656 |
| Net working capital | $19,832 | $11,159 | $ 6,466 | $ 3,072 | $ 2,138 | | $ 9,967 | $12,385 | |
| Change | –5,776 | –8,673 | –4,693 | –3,394 | –934 | $23,471 | 7,829 | 2,418 | $10,247 |
| Investments | $ 38 | $ 30 | $ 11 | $ 178 | $ 152 | $ 113 | $ 143 | $ 202 | |
| Change | –0– | –8 | –19 | 167 | –26 | | –9 | 59 | $ 50 |
| Deferred charges | $ 435 | $ 610 | $ 484 | $ 545 | $ 407 | | $ 414 | $ 389 | |
| Change | –512 | 175 | –126 | 61 | –138 | $ 540 | 7 | –25 | $ –18 |
| Sundry assets | $ –0– | $ 1,046 | $ –0– | $ –0– | $ –0– | | $ –0– | $ –0– | |
| Change | | 1,046 | –1,046 | | | $ –0– | | | $ –0– |
| Plant assets | $51,896 | $53,501 | $49,358 | $49,792 | $49,421 | | $49,163 | $48,662 | |
| Allowance for depreciation | 21,723 | 24,163 | 23,744 | 25,352 | 26,853 | | 28,191 | 28,654 | |
| Net plant assets | $30,173 | $29,338 | $25,614 | $24,440 | $22,568 | | $20,972 | $20,008 | |
| Change | –3,104 | –835 | –3,724 | –1,174 | –1,872 | $10,708 | –1,596 | –964 | $–2,559 |
| Net investment or disinvestment | $–9,392 | $–8,295 | $–9,608 | $–4,340 | $–2,970 | $34,606 | $ 6,231 | $ 1,488 | $ 7,720 |

# APPENDIX III A

## Selected Examples of Companies that Paid Dividends Materially in Excess of Depression Earnings

The *earning deficiency* reported arises when net income is less than interest and dividend payments. In case a company operated at a loss, payment of interest and dividends added to losses gives the earning deficiency. The reported deficiency does not represent a loss of current funds because expense and expenditure may differ greatly.

*Adjusted earning deficiency* includes surplus and net worth reserve adjustments, some of which involve funds while others do not. Assets changed each period by the amount of adjusted retained earnings and represent long run business profits or losses, provided cost figures were kept in the accounts. The adjusted figures do not necessarily imply that funds were made available or depleted within the particular period, however.

The vital question is, how did these companies meet the expenses, losses, and interest and dividend payments which were in excess of the current revenue produced? Which assets were liquidated to provide the funds? It is impossible to arrive at precise figures from data contained in reports to stockholders, but the procedure followed shows the relative amounts of liquidation in the various assets which provided funds to meet the earning deficiencies.

The financial summary of each company is based upon balance sheet figures at important stages in the cycle. Assets were liquidated during the depression and the *net liquidation* is therefore an *adjusted earning deficiency*. In simple language, had earnings been great enough there would be no liquidation of assets. Hence, asset liquidation, either by explicit transaction or write-downs, needs to be accounted for. In most cases we can point out the approximate nonfund adjustments and by the process of elimination arrive at the amount of funds provided to meet the deficiency resulting from lack of adequate revenue.

In the tables of Chapter 3 the *adjusted income after interest* includes only those adjustments to surplus reserves which seem clearly to involve accumulation or liquidation of funds during the period that affect dividend paying ability, whereas the financial summaries in Appendix III are designed to account for all book values.

**Financial Summary**
**Sears, Roebuck & Company**
**(In thousands of dollars)**

**Earning Deficiency Adjusted, 1931–32, $ 23,823**
**Earning Deficiency Reported, 1931–32, $ 8,626**
**Retained Earnings Reported,* 1922–30, $106,939**
**Retained Earnings Adjusted, 1922–30, $107,009**

| Item | 1921 | | 1930 | | 1932 | | 1931–32 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 10,868 | 11.9 | $ 9,868 | 10.4 | $ 7,630 | 15.2 | $ −2,238 |
| Liquid securities | 11,286 | 12.4 | 17,695 | 18.6 | 5,519 | 11.0 | −12,176† |
| Receivables | 52,579 | 57.8 | 37,248 | 39.1 | 20,097 | 40 1 | −17,151‡ |
| Inventories | 53,327 | 58.7 | 63,501 | 66.6 | 52,027 | 103.9 | −11,474 |
| Total current assets | $128,060 | 140.9 | $128,312 | 134.6 | $ 85,273 | 170.2 | $−43,039 |
| Current liabilities§ | 37,157 | 40.9 | 32,984 | 34.6 | 35,177 | 70.2 | +2,194 |
| Net working capital | $ 90,903 | 61.5 | $ 95,328 | 47.4 | $ 50,096 | 28.5 | $−45,233 |
| Securities | 3,932 | 2.7 | 5,583 | 2.8 | 33,175 | 18.9 | 27,591 |
| Sundry assets | | | 4,972 | 2.5 | 4,000 | 2.3 | −972 |
| Intangibles | 30,000 | 20.3 | 10,000 | 5.0 | 10,000 | 5.7 | −0− |
| Plant assets | 22,928 | 15.5 | 85,098 | 42.3 | 78,398 | 44.6 | −0− |
| Total | $147,703 | 100.0 | $200,982 | 100.0 | $175,668 | 100.0 | $−18,614 |
| Unexpended depreciation | | | | | | | 6,700 |
| Total liquidation | | | | | | | $ 25,314 |
| Stock retired | | | | | | | 1,491 |
| Deficiency accounted for | | | | | | | $ 23,823 |
| Surplus reserves// | $ 6,365 | | $ 82,282 | | $ 56,068 | | $−26,214 |
| Losses | | | | | −0− | | |
| Interest and dividends | | | | | 8,626 | | |
| Write-downs and adjustments | | | | | 17,588 | | |
| | | | | | $ 82,282 | | |

* 63 per cent of total net income.
† Write-down, $6,533.
‡ Loss on collections, $3,733.
§ Note that current liabilities became relatively a much greater equity by 1932.
// Includes $2,392,000 stock dividends.

### FINANCIAL SUMMARY
### American Tobacco Company
### (In thousands of dollars)

Earning Deficiency Adjusted, 1933–36, $21,438
Earning Deficiency Reported, 1933–36, $19,216
Retained Earnings Reported,* 1922–32, $74,731
Retained Earnings Adjusted, 1922–32, $73,906

| Item | 1921 | | 1932 | | 1936 | | 1933–36 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 10,854 | 12 | $ 46,460 | 28 | $ 19,502 | 13 | $–26,958 |
| Receivables | 12,151 | 13 | 16,100 | 10 | 13,597 | 9 | –2,503 |
| Inventories | 78,936 | 86 | 114,687 | 70 | 122,398 | 85 | 7,711 |
| Total current assets | $101,941 | 111 | $177,247 | 108 | $155,497 | 107 | $–21,750 |
| Current liabilities | 10,296 | –11 | 13,293 | –8 | 10,698 | –7 | –2,596 |
| Net working capital | $ 91,644 | 51 | $163,954 | 56 | $144,799 | 51 | $–19,154 |
| Investments | 25,219 | 14 | 51,773 | 18 | 28,206 | 10 | –23,568 |
| Intangibles | 54,099 | 30 | 54,099 | 19 | 90,848 | 32 | 36,749† |
| Plant assets | 9,203 | 5 | 20,502 | 7 | 17,609 | 7 | –0– |
| Total | $180,165 | 100 | $290,328 | 100 | $281,462 | 100 | $ –5,973 |
| Unexpended depreciation | | | | | | | 2,893 |
| Total liquidation | | | | | | | $ 8,866 |
| New security issues | | | | | | | 12,570 |
| Deficiency accounted for | | | | | | | $ 21,436 |
| Surplus reserves† | $ 14,750 | | $118,116 | | $ 59,930 | | $–58,186† |
| Losses | | | | | –0– | | |
| Interest and dividends | | | | | 19,215 | | |
| Write-downs and adjustments† | | | | | 38,971 | | |
| | | | | | $118,116 | | |
| Add: Cost of brand name charged to surplus | | | | | | | 36,749 |
| | | | | | | | $ 21,437 |

* 24 per cent of total net income.

† The company charged this item to earned surplus, but cash was paid for the brand names and there appears to be ample reason to regard the expenditure as a valid capital asset.

### FINANCIAL SUMMARY
### General Electric Company
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–33, $ 96,066
Earning Deficiency Reported, 1931–33, $ 38,926
Retained Earnings Reported,* 1922–30, $130,432
Retained Earnings Adjusted, 1922–30, $186,927

| Item | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 39,889 | 26 | $141,718 | 70 | $ 60,902 | 38 | $–80,816 |
| Liquid securities | 23,863 | 16 | –0– | –0– | 50,977 | 32 | 50,977 |
| Receivables | 54,830 | 36 | 41,677 | 21 | 18,341 | 11 | –23,336 |
| Inventories | 74,447 | 50 | 76,769 | 38 | 49,220 | 30 | –27,549 |
| Total current assets | $192,029 | 128 | $260,164 | 128 | $179,440 | 111 | $ 80,724 |
| Current liabilities | 42,704 | 28 | 57,726 | 28 | 17,830 | 11 | –39,897 |
| Net working capital | $150,325 | 50 | $202,438 | 45 | $161,610 | 44 | $–40,827 |
| Investments | 75,326 | 26 | 204,810 | 45 | 154,682 | 43 | –50,128† |
| Sundry assets | 1,697 | 1 | 253 | –0– | 2,672 | 1 | 2,421 |
| Plant assets | 66,957 | 23 | 45,868 | 10 | 42,242 | 12 | –0– |
| Total | $294,305 | 100 | $453,368 | 100 | $361,207 | 100 | $ 88,534 |
| Unexpended depreciation | | | | | | | 3,625 |
| Total liquidation | | | | | | | $ 92,159 |
| Long term debt issued | | | | | | | 3,905 |
| Deficiency accounted for | | | | | | | $ 96,064 |
| Surplus reserves | $ 84,106 | | $228,105 | | $132,039 | | $–96,066 |
| Losses | | | | | –0– | | |
| Interest and dividends | | | | | 38,926‡ | | |
| Write-downs and sundry adjustments | | | | | 57,139 | | |
| | | | | | $228,105 | | |

* 31 per cent of total net income.
† Write-down.
‡ Includes $26,440 RCA stock.

**Financial Summary**
**Chrysler Corporation**
**(In thousands of dollars)**

Earning Deficiency Adjusted, 1930–32, $35,377
Earning Deficiency Reported, 1930–32, $29,420
Retained Earnings Reported,* 1922–29, $65,935
Retained Earnings Adjusted, 1922–29, $73,938

| Item | 1921 Amount | 1921 Per Cent | 1929 Amount | 1929 Per Cent | 1932 Amount | 1932 Per Cent | 1930–32 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| Cash | $ 2,895 | 21 | $ 36,978 | 50 | $ 33,736 | 66 | $ –3,242 |
| Liquid securities | 4,121 | 30 | 1,730 | 2 | 8,867 | 17 | 7,137 |
| Receivables | 2,151 | 16 | 13,503 | 18 | 4,702 | 9 | –8,801 |
| Inventories | 10,936 | 79 | 39,987 | 54 | 20,205 | 40 | –19,782 |
| Total current assets | $20,103 | 146 | $ 92,198 | 124 | $ 67,510 | 132 | $–24,688 |
| Current liabilities | 6,279 | 45 | 18,928 | 26 | 16,395 | 32 | –2,532 |
| Net working capital | $13,824 | 24 | $ 73,270 | 38 | $ 51,115 | 42 | $–22,156 |
| Investments | 983 | 2 | 8,920 | 5 | 9,180 | 7 | 260 |
| Sundry assets | –0– | | –0– | | –0– | | –0– |
| Intangibles | 25,030 | 44 | 25,000 | 13 | –0– | | –25,000† |
| Plant assets | 16,678 | 30 | 83,624 | 44 | 61,697 | 51 | –0– |
| Total | $56,515 | 100 | $190,814 | 100 | $121,991 | 100 | $ 21,896 |
| Unexpended depreciation | | | | | | | 21,928 |
| Total liquidation | | | | | | | $ 43,824 |
| Debt and stock retired | | | | | | | 8,447 |
| Deficiency accounted for | | | | | | | $ 35,377 |
| Surplus reserves | $ 613 | | $ 67,292 | | $ 31,916 | | $–35,376 |
| Losses | | | | | 9,551 | | |
| Interest and dividends | | | | | 19,867 | | |
| Sundry | | | | | 5,958 | | |
| | | | | | $ 67,292 | | |

* 59 per cent of total net income.
† Write-off.

### Financial Summary
### Firestone Tire & Rubber Company
### (In thousands of dollars)

Earning Deficiency Adjusted, 1930–33, $11,188
Earning Deficiency Reported, 1930–33, $ 5,418*
Retained Earnings Reported,† 1922–29, $43,221
Retained Earnings Adjusted, 1922–29, $35,226

| Item | 1921 | | 1929 | | 1933 | | 1930–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 5,889 | 96 | $ 30,039 | 38 | $ 14,320 | 28 | $–15,719 |
| Liquid securities | –0– | | –0– | | –0– | | –0– |
| Receivables | 12,181 | 198 | 17,188 | 22 | 13,905 | 28 | –3,283 |
| Inventories | 12,534 | 203 | 41,360 | 52 | 28,816 | 57 | –12,544 |
| Total current assets | $30,604 | 497 | $ 88,586 | 112 | $ 57,042 | 113 | $–31,546 |
| Current liabilities | 24,443 | 397 | 8,537 | 11 | 6,563 | 13 | –1,974 |
| Net working capital | $ 6,161 | 15 | $ 80,049 | 52 | $ 50,478 | 41 | $-29,572 |
| Investments | 7,433 | 18 | 11,516 | 8 | 9,443 | 8 | –2,045 |
| Sundry assets | 6,617 | 16 | 10,461 | 7 | 4,095 | 3 | –6,394 |
| Intangibles | –0– | | –0– | | –0– | | –0– |
| Plant assets | 21,553 | 51 | 51,084 | 33 | 58,945 | 48 | 7,861 |
| Total | $41,764 | 100 | $153,110 | 100 | $122,962 | 100 | $ 30,150 |
| Unexpended depreciation | | | | | | | –0– |
| Total liquidation | | | | | | | $ 30,150 |
| Stock and debt retired | | | | | | | 18,959 |
| Deficiency accounted for | | | | | | | $ 11,191 |
| Surplus reserves | $16,873 | | $ 47,954 | | $ 36,615 | | $–11,339 |
| Losses | | | | | –0– | | |
| Interest and dividends | | | | | 4,638 | | |
| Sundry | | | | | 6,701 | | |
| | | | | | $ 47,954 | | |

* $4,825 charged to net worth reserves.
† 58 per cent of total net income.

# APPENDIX III B

## Selected Examples of Companies that Paid Dividends after Losses

### Financial Summary
### International Harvester Company
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–34, $29,411
Earning Deficiency Reported, 1931–34, $49,486
Retained Earnings Reported,* 1922–30, $81,832
Retained Earnings Adjusted, 1922–30, $94,105

| Item | 1921 | | 1930 | | 1934 | | 1931–34 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 8,362 | 5 | $ 27,643 | 12 | $ 28,807 | 14 | $ 1,164 |
| Marketable securities | 823 | 1 | 2,653 | 1 | 34,311 | 17 | 31,658 |
| Receivables | 56,283 | 37 | 136,075 | 61 | 70,183 | 35 | –65,892 |
| Inventories | 114,086 | 75 | 90,738 | 40 | 92,268 | 45 | –1,530 |
| Total current assets | $179,554 | 118 | $257,109 | 114 | $225,569 | 111 | $–31,540 |
| Current liabilities | 27,508 | 18 | 31,641 | 14 | 22,387 | 11 | –9,255 |
| Net working capital | $152,046 | 63 | $225,468 | 64 | $203,182 | 64 | $–22,285 |
| Investments | –0– | –0– | 8,432 | 2 | 8,812 | 2 | 379 |
| Sundry assets | 4,087 | 2 | 551 | –0– | 547 | –0– | –4 |
| Intangibles | –0– | | –0– | | –0– | | –0– |
| Plant assets | 83,030 | 35 | 117,708 | 34 | 104,341 | 34 | |
| Total | $239,163 | 100 | $352,159 | 100 | $316,882 | 100 | |
| Unexpended depreciation | | | | | | | 13,368 |
| Total liquidation | | | | | | | $ 35,278 |
| New capital issues | | | | | | | –5,867 |
| Deficiency accounted for | | | | | | | $ 29,411 |
| Surplus reserves | $ 82,932 | | $ 94,789 | | $ 65,378 | | $–29,411 |
| Losses | | | | | 5,295 | | |
| Interest and dividends | | | | | 45,312 | | |
| Sundry adjustments | | | (increase)† | | 21,196 | | |
| | | | | | $ 94,789 | | |

* 44 per cent of total net income.
† Secret reserve for inventory prices restored to surplus.

## Financial Summary

### Westinghouse Electric & Manufacturing Company

### (In thousands of dollars)

**Earning Deficiency Adjusted, 1931–33, $55,414**
**Earning Deficiency Reported, 1931–33, $38,576**
**Retained Earnings Reported,* 1922–30, $62,458**
**Retained Earnings Adjusted, 1922–30, $49,820**

| Item | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 10,031 | 11 | $ 24,119 | 24 | $ 14,468 | 20 | $ -9,651 |
| Marketable securities | 7,886 | 9 | 8,541 | 8 | 12,719 | 18 | 4,178 |
| Receivables | 23,808 | 28 | 37,206 | 37 | 16,591 | 24 | -20,615 |
| Inventories | 55,890 | 65 | 46,331 | 46 | 32,983 | 46 | -13,348 |
| Total current assets | $ 97,615 | 113 | $116,198 | 115 | $ 76,761 | 108 | $-39,436 |
| Current liabilities | 11,400 | 13 | 15,187 | 15 | 5,451 | 8 | -9,736 |
| Net working capital | $ 86,215 | 55 | $101,011 | 44 | $ 71,310 | 41 | $-29,700 |
| Investments | 17,029 | 11 | 57,682 | 25 | 36,904 | 21 | -20,779† |
| Sundry assets | | | | | | | |
| Intangible assets | 4,483 | 3 | -0- | | -0- | | -0- |
| Plant assets | 47,943 | 31 | 72,272 | 31 | 67,199 | 38 | -0- |
| Total | $155,670 | 100 | $230,965 | 100 | $175,413 | 100 | $-50,479 |
| Unexpended depreciation | | | | | | | 5,073 |
| Total liquidation | | | | | | | $ 55,552 |
| New capital issues | | | | | | | -139 |
| Deficiency accounted for | | | | | | | $ 55,413 |
| Surplus reserves | $ 44,608 | | $ 97,650 | | $ 42,237 | | $-55,413 |
| Losses | | | | | 21,197 | | |
| Interest and dividends | | | | | 17,380 | | |
| Write-downs and sundry adjustments | | | | | 16,836 | | |
| | | | | | $ 97,650 | | |

* 29 per cent of total net income.
† Write-down $16,233,000.

**FINANCIAL SUMMARY**
**B. F. Goodrich Company**
**(In thousands of dollars)**

Earning Deficiency Adjusted, 1930–33, $35,520
Earning Deficiency Reported, 1930–33, $25,231
Retained Earnings Reported,* 1922–29, $22,775
Retained Earnings Adjusted, 1922–29, $12,364

| Item | 1921 | | 1929 | | 1933 | | 1930–33 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 2,574 | 5 | $ 10,501 | 18 | $ 9,309 | 21 | $ −1,192 |
| Marketable securities | 43 | 1 | –0– | | 2,782 | 6 | 2,782 |
| Receivables | 19,408 | 39 | 33,739 | 57 | 15,649 | 35 | −18,090 |
| Inventories | 30,213 | 62 | 46,285 | 79 | 25,901 | 57 | −20,384 |
| Total current assets | $52,238 | 107 | $ 90,525 | 154 | $ 53,642 | 119 | $−36,883 |
| Current liabilities | 3,621 | 7 | 31,605 | 54 | 8,426 | 19 | −23,178 |
| Net working capital | $48,617 | 57 | $ 58,920 | 45 | $ 45,216 | 43 | $−13,706 |
| Investments | 4,447 | 5 | 2,466 | 2 | 15,472 | 14 | 13,007 |
| Sundry assets | –0– | | 1,752 | 1 | 688 | 1 | −1,065 |
| Intangible assets | | | | | | | |
| Plant assets | 32,116 | 38 | 67,600 | 52 | 44,587 | 42 | −14,373 |
| Total | $85,180 | 100 | $130,737 | 100 | $105,963 | 100 | $−16,137 |
| Unexpended depreciation | | | | | | | 8,639 |
| Total liquidation | | | | | | | $ 24,776 |
| New capital issues | | | | | | | 10,746 |
| Deficiency accounted for | | | | | | | $ 35,522 |
| Surplus reserves | $16,873 | | $ 28,202 | | $ −1,942 | | $−30,144† |
| Losses | | | | | 8,808 | | |
| Interest and dividends | | | | | 14,957 | | |
| Write-downs and sundry adjustments | | | | | 6,379 | | |
| | | | | | $ 28,202 | | |

* 30 per cent of total net income.
† Discrepancy due to stock issues and revaluations.

### Financial Summary
### United States Steel Corporation
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–34, $246,840
Earning Deficiency Reported, 1931–34, $213,638
Retained Earnings Reported,* 1922–30, $332,577
Retained Earnings Adjusted, 1922–30, $342,392

| Item | 1921 | | 1930 | | 1934 | | 1931–34 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 123,781 | 25 | $ 126,741 | 27 | $ 71,305 | 19 | $ –55,436 |
| Marketable securities | 131,463 | 27 | 71,066 | 15 | 54,626 | 15 | –16,440 |
| Receivables | 72,683 | 15 | 57,513 | 12 | 36,832 | 10 | –20,681 |
| Inventories | 241,504 | 50 | 323,053 | 69 | 257,360 | 71 | –65,693 |
| Total current assets | $ 569,431 | 117 | $ 578,373 | 123 | $ 420,122 | 115 | $–158,210 |
| Current liabilities | 84,249 | 17 | 108,873 | 23 | 55,987 | 15 | –52,887 |
| Net working capital | $ 485,182 | 22 | $ 469,500 | 21 | $ 364,135 | 17 | $–105,363 |
| Investments | 14,173 | 1 | 20,692 | 1 | 16,358 | 1 | –4,333 |
| Sundry assets | 54,799 | 2 | 51,336 | 2 | 13,259 | 1 | –38,077 |
| Intangible assets | 55,907 | 2 | 66,816 | 3 | 8,229 | 1 | –58,587 |
| Plant assets | 1,644,795 | 73 | 1,677,327 | 73 | 1,626,144 | 80 | –21,000† |
| Total | $2,254,856 | 100 | $2,285,671 | 100 | $2,028,126 | 100 | $ 227,360 |
| Unexpended depreciation | | | | | | | 30,184 |
| Total liquidation | | | | | | | $ 257,544 |
| Capital retired | | | | | | | 10,705 |
| Deficiency accounted for | | | | | | | $ 246,839 |
| Surplus reserves | $ 813,758 | | $ 845,310 | | $ 598,469 | | $–246,841 |
| Losses | | | | | 95,308 | | |
| Interest and dividends | | | | | 118,331 | | |
| Write-downs and sundry adjustments | | | | | 33,202 | | |
| | | | | | $ 845,310 | | |

* 30 per cent of total net income.
† Write-down $21,000.

FINANCIAL SUMMARY
Hudson Motor Car Company
(In thousands of dollars)

Earning Deficiency Adjusted, 1929–34, $33,964
Earning Deficiency Reported, 1929–34, $22,859
Retained Earnings Reported,* 1922–29, $46,970
Retained Earnings Adjusted, 1922–29, $47,469

| Item | 1921 | | 1929 | | 1934 | | 1929–34 Increase or Decrease |
|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | |
| Cash | $ 1,290 | 44 | $ 4,760 | 19 | $ 2,576 | 120 | $ –2,184 |
| Marketable securities | –0– | | 12,385 | 48 | –0– | | –12,385 |
| Receivables | 1,041 | 35 | 3,862 | 15 | 745 | 35 | –3,117 |
| Inventories | 3,558 | 120 | 13,467 | 53 | 4,955 | 232 | –8,512 |
| Total current assets | $ 5,888 | 199 | $34,474 | 135 | $ 8,276 | 387 | $–26,198 |
| Current liabilities | 2,926 | 99 | 8,865 | 35 | 6,138 | 287 | 2,727 |
| Net working capital | $ 2,962 | 24 | $25,608 | 43 | $ 2,138 | 8 | $–23,471 |
| Investments | 79 | 1 | 38 | –0– | 152 | 1 | 114 |
| Sundry assets | 162 | 1 | 947 | 2 | 407 | 2 | –540 |
| Intangible assets | | | | | | | |
| Plant assets | 9,059 | 74 | 33,276 | 55 | 22,567 | 89 | –5,264 |
| Total | $12,262 | 100 | $59,870 | 100 | $25,264 | 100 | $–29,161 |
| Unexpended depreciation | | | | | | | 5,445 |
| Total liquidation | | | | | | | $ 34,606 |
| New security issues | | | | | | | –641 |
| Deficiency accounted for | | | | | | | $ 33,965 |
| Surplus reserves | $ 9,775 | | $39,912 | | $ 5,947 | | |
| Losses | | | | | 14,640 | | |
| Interest and dividends | | | | | 8,219 | | |
| Write-downs and sundry adjustments | | | | | 11,106 | | 33,965 |
| | | | | | $39,912 | | |

* 52 per cent of total net income.

# APPENDIX III C

## Selected Examples of Companies that Paid No Depression Dividends

### Financial Summary
### American Cyanamid & Chemical Corporation
### (In thousands of dollars)

Retained Earnings Adjusted, 1931–33, †$3,529
Retained Earnings Reported, 1931–33, †$3,339
Retained Earnings Reported,* 1922–30, $5,858
Retained Earnings Adjusted, 1922–30, $2,347

| Item | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease | Liquidation |
|---|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | | |
| Cash | $ 380 | 19 | $ 2,533 | 14 | $ 5,847 | 38 | $ 3,314 | 13% |
| Marketable securities | 50 | 2 | 3,272 | 18 | 255 | 2 | −3,017 | −92 |
| Receivables | 136 | 7 | 4,917 | 26 | 3,918 | 25 | −999 | −20 |
| Inventories | 1,901 | 96 | 12,771 | 69 | 9,863 | 64 | −2,908 | −23 |
| Total current assets | $ 2,469 | 125 | $23,492 | 126 | $19,883 | 128 | $ −3,609 | −15% |
| Current liabilities | 500 | 25 | 4,878 | 26 | 4,362 | 28 | −516 | −11 |
| Net working capital | $ 1,969 | 12 | $18,614 | 23 | $15,522 | 33 | $ −3,094 | −17% |
| Investments | 5,280 | 32 | 1,621 | 2 | 5,791 | 12 | 4,170 | |
| Sundry assets | | | 2,530 | 3 | | | −2,530 | |
| Intangible assets | 4,821 | 30 | 17,130 | 21 | 5,000 | 10 | −12,130† | |
| Plant assets | 4,242 | 26 | 42,535 | 51 | 21,383 | 45 | −21,151† | |
| Total | $16,312 | 100 | $82,429 | 100 | $47,695 | 100 | $ 34,734 | |
| Unexpended depreciation | | | | | | | | |
| Total liquidation | | | | | | | $ 34,734 | |
| Capital stock write-down | | | | | | | 28,558† | |
| Capital surplus reduction | | | | | | | 10,749† | |
| Debt increase | | | | | | | 1,045 | |
| Net capital adjustment | | | | | | | $ 38,262 | |
| Excess of capital write-down over asset decrease (retained earnings) | | | | | | | $ 3,528 | |
| Surplus reserves | $ 3,291 | | $ 4,197 | | $ 7,724 | | $ 3,527 | |
| Reported income retained | | | | | 3,339 | | | |
| Dividends and interest | | | | | −0− | | | |
| Sundry adjustments | | | | | 188 | | | |
| | | | | | $ 4,197 | | | |

* 36 per cent of total net income.
† Write-down against capital stock.

### Financial Summary
### Baldwin Locomotive Works
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–33, $14,639
Earning Deficiency Reported, 1931–33, $12,759
Retained Earnings Reported,* 1922–33, $ 7,231
Retained Earnings Adjusted, 1922–33, $ 66

| Item | 1921 | | 1930 | | 1933 | | 1931–33 Increase or Decrease | Liquidation |
|---|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | | |
| Cash | $ 2,056 | 6 | $13,454 | 61 | $ 7,649 | 58 | $ –5,805 | –43% |
| Marketable securities | 24,392 | 71 | 1,058 | 5 | 234 | 2 | –824 | –78 |
| Receivables | 17,134 | 50 | 5,349 | 24 | 1,853 | 14 | –3,496 | –65 |
| Inventories | 5,161 | 15 | 8,689 | 39 | 5,266 | 40 | –3,423 | –39 |
| Total current assets | $48,743 | 142 | $28,549 | 129 | $15,001 | 113 | $–13,548 | –47% |
| Current liabilities | 14,379 | 42 | 6,459 | 29 | 1,768 | 13 | –4,691 | –72 |
| Net working capital | $34,364 | 51 | $22,090 | 24 | $13,233 | 17 | $ –8,857 | –40% |
| Investments | 4,429 | 7 | 12,824 | 14 | 6,175 | 8 | –6,649 | –52 |
| Sundry assets | 1,678 | 2 | 5,898 | 6 | 7,306 | 9 | 1,408 | 24 |
| Intangible assets | | | | | | | | |
| Plant assets | 27,079 | 40 | 52,880 | 56 | 50,406 | 66 | | |
| Total | $67,550 | 100 | $93,692 | 100 | $77,120 | 100 | $ 14,098 | |
| Unexpended depreciation | | | | | | | 2,474 | |
| Total liquidation | | | | | | | $ 16,572 | |
| Capital retired | | | | | | | 1,935 | |
| Deficiency accounted for | | | | | | | $ 14,637 | |
| Surplus reserves | $17,552 | | $23,706 | | $ 9,251 | | | |
| Losses | | | | | 8,642 | | $–14,455† | |
| Dividends and interest ($3,416 interest) | | | | | 4,116 | | | |
| Write-downs and adjustments | | | | | 1,697 | | | |
| | | | | | $23,706 | | | |

* 18 per cent of total net income.
† Difference of $182,000 due to revaluation of common stock and charges to created capital surplus.

### FINANCIAL SUMMARY
### Chicago Pneumatic Tool Company
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–34, $ 507
Earning Deficiency Reported, 1931–34, $ 931
Retained Earnings Reported,* 1922–30, $3,144
Retained Earnings Adjusted, 1922–30, $ –51

| Item | 1921 | | 1930 | | 1934 | | 1931–34 Increase or Decrease | Liquidation |
|---|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | | |
| Cash | $ 546 | 7 | $ 446 | 6 | $ 305 | 5 | $ –141 | –32% |
| Marketable securities | 11 | | | | | | | |
| Receivables | 1,017 | 12 | 2,044 | 27 | 1,729 | 27 | –315 | –15 |
| Inventories | 8,167 | 98 | 6,976 | 91 | 5,891 | 90 | –1,085 | –16 |
| Total current assets | $ 9,741 | 117 | $ 9,466 | 124 | $ 7,924 | 122 | $ –1,542 | –16% |
| Current liabilities | 1,405 | 17 | 1,801 | 24 | 1,407 | 22 | –395 | –21 |
| Net working capital | $ 8,335 | 48 | $ 7,665 | 40 | $ 6,518 | 37 | $ –1,146 | –15% |
| Investments | 33 | | 277 | 2 | 483 | 3 | 205 | 74 |
| Sundry assets | | | | | | | | |
| Intangible assets | | | | | | | | |
| Plant assets | 8,922 | 52 | 10,967 | 58 | 10,272 | 60 | | 6 |
| Total | $17,290 | 100 | $18,909 | 100 | $17,272 | 100 | $ 941 | |
| Unexpended depreciation | | | | | | | 695 | |
| Total liquidation | | | | | | | $ 1,637 | |
| Capital retired | | | | | | | 1,129 | |
| Deficiency accounted for | | | | | | | $ 508 | |
| Surplus reserves | $ 4,642 | | $ 4,593 | | $ 4,085 | | $ –508 | |
| Losses | | | | | 68 | | | |
| Interest | | | | | 864 | | | |
| Sundry adjustments | | | | | +424 | | | |

* 33 per cent of total net income.

FINANCIAL SUMMARY
United States Rubber Company
(In thousands of dollars)

Earning Deficiency Adjusted, 1930–33, $49,668
Earning Deficiency Reported, 1930–33, $25,563
Retained Earnings Reported,* 1922–29, $36,344
Retained Earnings Adjusted, 1922–29, $16,232

| Item | 1921 | | 1929 | | 1933 | | 1930–33 Increase or Decrease | Liquidation |
|---|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | | |
| Cash | $ 12,999 | 16 | $ 16,800 | 21 | $ 8,054 | 20 | $ -8,746 | -52% |
| Marketable securities | | | | | 139 | | 139 | --- |
| Receivables | 43,714 | 52 | 42,453 | 53 | 16,653 | 42 | -25,800 | -61 |
| Inventories | 76,942 | 92 | 57,500 | 72 | 25,254 | 64 | -32,246 | -56 |
| Total current assets | $133,655 | 160 | $116,752 | 147 | $ 50,099 | 127 | $-66,653 | -57% |
| Current liabilities | 49,931 | 60 | 37,304 | 47 | 10,778 | 27 | -36,525 | -71 |
| Net working capital | $ 83,724 | 31 | $ 79,448 | 29 | $ 39,321 | 26 | $-40,128 | -62% |
| Investments | 9,068 | 3 | 27,103 | 10 | 33,413 | 22 | 6,310 | 23 |
| Sundry assets | 11,273 | 4 | 3,727 | 1 | 1,623 | 1 | -2,105 | -56 |
| Intangible assets | | | 58,925 | 22 | | | -58,925† | |
| Plant assets | 169,657 | 62 | 101,384 | 48 | 77,586 | 51 | | |
| Total | $273,722 | 100 | $270,588 | 100 | $151,943 | 100 | $ 35,922 | |
| Unexpended depreciation | | | | | | | 23,798 | 23 |
| Total liquidation | | | | | | | $ 59,720 | |
| Capital retired | | | | | | | 10,052 | |
| Deficiency accounted for | | | | | | | $ 49,668 | |
| Surplus reserves | $ 41,383 | | $ 25,152 | | $-24,514 | | $-49,666 | |
| Losses | | | | | 10,767 | | | |
| Interest | | | | | 14,852 | | | |
| Write-downs | | | | | 24,047 | | | |

* 32 per cent of total net income.
† Adjustment, $-58,925 omitted in totals.

### FINANCIAL SUMMARY
### Republic Steel Corporation
### (In thousands of dollars)

Earning Deficiency Adjusted, 1931–34, $32,395
Earning Deficiency Reported, 1931–34, $26,456
Retained Earnings Reported,* 1922–30, $ 5,424
Retained Earnings Adjusted, 1922–30, $ 7,058

| Item | 1921 | | 1930 | | 1934 | | 1931–34 Increase or Decrease | Liquidation |
|---|---|---|---|---|---|---|---|---|
| | Amount | Per Cent | Amount | Per Cent | Amount | Per Cent | | |
| Cash | $ 1,292 | 8 | $ 8,628 | 21 | $ 6,505 | 22 | $ –2,123 | –25% |
| Marketable securities | | | | | | | | |
| Receivables | 3,686 | 24 | 9,633 | 23 | 7,772 | 26 | –1,861 | –19 |
| Inventories | 16,719 | 110 | 38,997 | 94 | 28,981 | 98 | –10,016 | –26 |
| Total current assets | $ 21,698 | 143 | $ 57,258 | 138 | $ 43,258 | 147 | $–14,000 | –24% |
| Current liabilities | 6,517 | 43 | 15,877 | 38 | 13,751 | 47 | –2,127 | –13 |
| Net working capital | $ 15,180 | 15 | $ 41,381 | 14 | $ 29,507 | 12 | $–11,873 | –29% |
| Investments | 1,910 | 2 | 19,648 | 7 | 18,294 | 7 | –1,354 | –7 |
| Sundry assets | 1,452 | 1 | 1,575 | 1 | 1,079 | | –496 | –31 |
| Intangible assets | | | | | | | | |
| Plant assets | 81,754 | 82 | 230,020 | 78 | 199,857 | 81 | | |
| Total | $100,296 | 100 | $292,624 | 100 | $248,737 | 100 | $ 13,723 | |
| Unexpended depreciation | | | | | | | 30,164 | |
| Total liquidation | | | | | | | $ 43,887 | |
| Capital retired | | | | | | | 11,493 | |
| Deficiency accounted for | | | | | | | $ 32,394 | |
| Surplus reserves | $ 31,939 | | $ 80,210 | | $ 48,011 | | $–32,199† | |
| Losses | | | | | 12,747 | | | |
| Dividends and interest ($13,278 interest) | | | | | 13,708 | | | |
| Write-downs and sundry | | | | | 5,744 | | | |
| | | | | | $ 80,210 | | | |

* 12 per cent of total net income.
† Capital surplus credits resulting from sale of treasury stock $195,000.

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# INDEX